

AMENDED IN ASSEMBLY MAY 15, 2003

AMENDED IN ASSEMBLY APRIL 30, 2003

AMENDED IN ASSEMBLY APRIL 24, 2003

CALIFORNIA LEGISLATURE—2003–04 REGULAR SESSION

ASSEMBLY BILL

No. 651

Introduced by Assembly Member Corbett

February 19, 2003

An act to add Article 1.8 (commencing with Section 52337) to Chapter 9 of Part 28 of the Education Code, and to amend Sections ~~6377, 17039, 17053.49, 23036, and 23649~~ of, and to add and repeal *17039 and 23036 of, and to add and repeal* Sections 17053.51 and 23651 of, the Revenue and Taxation Code, relating to taxation, and making an appropriation therefor, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 651, as amended, Corbett. Career Technical Education Campaign: ~~sales, use, income, and corporation taxes: manufacturer's investment.~~

Existing laws provide various programs relating to adult and career education.

This bill would declare the Legislature's intent that the State Department of Education establish the Career Technical Education Campaign for the purpose of encouraging businesses to make gifts of in-kind donations for career technical education in the state, as provided.

~~The Sales and Use Tax Law imposes a tax on the gross receipts from the sale in this state of, or the storage, use, or other consumption in this~~

~~state of, tangible personal property and provides various exemptions from the taxes imposed by that law. That law provides an exemption from those taxes for the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property, as defined, purchased for use by a qualified person, as defined, primarily in any state engaged in a new trade or business, as defined, of manufacturing, processing, refining, fabricating, or recycling of property, and introduced into the process, as specified. The~~

The Personal Income Tax Law and the Corporation Tax Law authorize various credits against the taxes imposed by those laws, including a credit against taxes imposed by those laws in an amount equal to 6% of the amount paid or incurred by the taxpayer during the taxable year for qualified property, as defined, that is placed in service in this state.

~~This bill would disallow the sales tax exemption unless the qualified person or taxpayer, as applicable, is certified as a participant in the Career Technical Education Campaign, as provided. This bill would reduce the income and corporation tax credit percentage from 6% to 1% over a 5-year period, as provided, and would eliminate those credits as of January 1, 2011. This~~

This bill would also allow, until January 1, 2012 from January 1, 2007, until January 1, 2014, similar new income and corporation tax credits, restricted to participants in the campaign, in increasing amounts from 2% 1% to 7% over a 5-year period, as specified.

~~This bill would result in a change in state taxes for the purpose of increasing state revenues within the meaning of Section 3 of Article XIII A of the California Constitution, and thus would require for passage the approval of $\frac{2}{3}$ of the membership of each house of the Legislature.~~

~~This bill would appropriate an unspecified amount from the General Fund to the Franchise Tax Board, as provided.~~

This bill would request that the University of California evaluate the effectiveness of the credit, as provided.

This bill would take effect immediately as a tax levy.

Vote: $\frac{2}{3}$ majority. Appropriation: yes-no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Article 1.8 (commencing with Section 52337) is added to Chapter 9 of Part 28 of the Education Code, to read:

Article 1.8. Career Technical Education Campaign

52337. It is the intent of the Legislature that the State Department of Education establish the Career Technical Education Campaign for the purpose of encouraging businesses to make gifts of in-kind donations for career technical education in the state. It is further the intent of the Legislature that the State Department of Education adopt rules and regulations in 2004 2006, to do the following:

(a) Establish procedures, processes, and criteria according to which a business may, for purposes of Sections 6377, 17053.51, and 23651 of the Revenue and Taxation Code, be considered a qualified participant in a campaign as described by this article.

(b) Establish the valuation mechanism that will determine if a taxpayer is a “qualified participant” for purposes of Sections 17053.51 and 23651 of the Revenue and Taxation Code.

(c) Certify qualified participants in a campaign as described by this article and provide a list of certified qualified participants to the Franchise Tax Board and the State Board of Equalization, as appropriate, in the manner most efficient for the department and those agencies.

~~SEC. 2. Section 6377 of the Revenue and Taxation Code is amended to read:~~

~~6377. (a) There are exempted from the taxes imposed by this part the gross receipts from the sale of, and the storage, use, or other consumption in this state of, any of the following:~~

~~(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point any raw materials are received by the qualified person and introduced into the process and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling has altered property to its completed form, including packaging, if required.~~

~~(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development.~~

~~(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in paragraph (1) or (2).~~

~~(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.~~

~~This exemption shall not apply to any tangible personal property that is used primarily in administration, general management, or marketing.~~

~~(b) For purposes of this section:~~

~~(1) "Fabricating" means to make, build, create, produce, or assemble components or property to work in a new or different manner.~~

~~(2) "Manufacturing" means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.~~

~~(3) "Primarily" means tangible personal property used 50 percent or more of the time in an activity described in subdivision (a).~~

~~(4) "Process" means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw~~

1 ~~materials are stored on the same premises where the qualified~~
2 ~~taxpayer's manufacturing, processing, refining, or recycling~~
3 ~~activity is conducted. Raw materials that are stored on premises~~
4 ~~other than where the qualified taxpayer's manufacturing,~~
5 ~~processing, refining, fabricating, or recycling activity is~~
6 ~~conducted, shall not be considered to have been introduced into the~~
7 ~~manufacturing, processing, refining, fabricating, or recycling~~
8 ~~process.~~

9 ~~(5) "Processing" means the physical application of the~~
10 ~~materials and labor necessary to modify or change the~~
11 ~~characteristics of property.~~

12 ~~(6) "Qualified person" means any person that is all of the~~
13 ~~following:~~

14 ~~(A) A new trade or business. In determining whether a trade or~~
15 ~~business activity qualifies as a new trade or business, the following~~
16 ~~rules shall apply:~~

17 ~~(i) In any case where a person purchases or otherwise acquires~~
18 ~~all or any portion of the assets of an existing trade or business~~
19 ~~(irrespective of the form of entity) that is doing business in this~~
20 ~~state (within the meaning of Section 23101), the trade or business~~
21 ~~thereafter conducted by that person (or any related person) shall~~
22 ~~not be treated as a new business if the aggregate fair market value~~
23 ~~of the acquired assets (including, real, personal, tangible, and~~
24 ~~intangible property) used by that person (or any related person) in~~
25 ~~the conduct of his or her trade or business exceed 20 percent of the~~
26 ~~aggregate fair market value of the total assets of the trade or~~
27 ~~business being conducted by the person (or any related person).~~
28 ~~For purposes of this subparagraph only, the following rules shall~~
29 ~~apply:~~

30 ~~(I) The determination of the relative fair market values of the~~
31 ~~acquired assets and the total assets shall be made as of the last day~~
32 ~~of the month following the quarterly period in which the person (or~~
33 ~~any related person) first uses any of the acquired trade or business~~
34 ~~assets in his or her business activity.~~

35 ~~(II) Any acquired assets that constituted property described in~~
36 ~~Section 1221(1) of the Internal Revenue Code in the hands of the~~
37 ~~transferor shall not be treated as assets acquired from an existing~~
38 ~~trade or business, unless those assets also constitute property~~
39 ~~described in Section 1221(1) of the Internal Revenue Code in the~~
40 ~~hands of the acquiring person (or related person).~~

1 (ii) ~~In any case where a person (or any related person) is~~
2 ~~engaged in one or more trade or business activities in this state, or~~
3 ~~has been engaged in one or more trade or business activities in this~~
4 ~~state within the preceding 36 months (“prior trade or business~~
5 ~~activity”), and thereafter commences an additional trade or~~
6 ~~business activity in this state, the additional trade or business~~
7 ~~activity shall only be treated as a new business if the additional~~
8 ~~trade or business activity is classified under a different division of~~
9 ~~the Standard Industrial Classification Manual published by the~~
10 ~~United States Office of Management and Budget, 1987 edition,~~
11 ~~than are any of the person’s (or any related person’s) current or~~
12 ~~prior trade or business activities in this state.~~

13 (iii) ~~In any case where a person, including all related persons,~~
14 ~~is engaged in trade or business activities wholly outside of this~~
15 ~~state and that person first commences doing business in this state~~
16 ~~(within the meaning of Section 23101) after December 31, 1993~~
17 ~~(other than by purchase or other acquisition described in clause~~
18 ~~(i)), the trade or business activity shall be treated as a new business.~~

19 (iv) ~~In any case where the legal form under which a trade or~~
20 ~~business activity is being conducted is changed, the change in form~~
21 ~~shall be disregarded and the determination of whether the trade or~~
22 ~~business activity is a new business shall be made by treating the~~
23 ~~person as having purchased or otherwise acquired all or any~~
24 ~~portion of the assets of an existing trade or business under the rules~~
25 ~~of clause (i).~~

26 (v) ~~“Related person” means any person that is related to that~~
27 ~~person under either Section 267 or 318 of the Internal Revenue~~
28 ~~Code.~~

29 (vi) ~~“Acquire” includes any gift, inheritance, transfer incident~~
30 ~~to divorce, or any other transfer, whether or not for consideration.~~

31 (B) ~~Engaged in those lines of business described in Codes 2011~~
32 ~~to 3999, inclusive, of the Standard Industrial Classification~~
33 ~~Manual published by the United States Office of Management and~~
34 ~~Budget, 1987 edition.~~

35 (C) ~~Certified, in the form and manner prescribed by the board,~~
36 ~~as a participant in the Career Technical Education Campaign~~
37 ~~pursuant to Section 52337 of the Education Code for the year for~~
38 ~~which an exemption is claimed under this section.~~

1 ~~(7) Notwithstanding paragraph (6), “qualified person” shall~~
2 ~~not include any person who has conducted business activities in a~~
3 ~~new trade or business for three or more years.~~

4 ~~(8) “Refining” means the process of converting a natural~~
5 ~~resource to an intermediate or finished product.~~

6 ~~(9) “Research and development” means those activities that~~
7 ~~are described in Section 174 of the Internal Revenue Code or in any~~
8 ~~regulations thereunder.~~

9 ~~(10) “Tangible personal property” does not include any of the~~
10 ~~following:~~

11 ~~(A) Consumables with a normal useful life of less than one~~
12 ~~year, except as provided in subparagraph (E) of paragraph (10).~~

13 ~~(B) Furniture, inventory, equipment used in the extraction~~
14 ~~process, or equipment used to store finished products that have~~
15 ~~completed the manufacturing process.~~

16 ~~(C) Any property for which a credit is claimed under either~~
17 ~~Section 17053.49 or 23649.~~

18 ~~(11) “Tangible personal property” includes, but is not limited~~
19 ~~to, all of the following:~~

20 ~~(A) Machinery and equipment, including component parts and~~
21 ~~contrivances such as belts, shafts, moving parts, and operating~~
22 ~~structures.~~

23 ~~(B) All equipment or devices used or required to operate,~~
24 ~~control, regulate, or maintain the machinery, including, without~~
25 ~~limitation, computers, data processing equipment, and computer~~
26 ~~software, together with all repair and replacement parts with a~~
27 ~~useful life of one or more years therefor, whether purchased~~
28 ~~separately or in conjunction with a complete machine and~~
29 ~~regardless of whether the machine or component parts are~~
30 ~~assembled by the taxpayer or another party.~~

31 ~~(C) Property used in pollution control that meets or exceed~~
32 ~~standards established by this state or any local or regional~~
33 ~~governmental agency within this state.~~

34 ~~(D) Special purpose buildings and foundations used as an~~
35 ~~integral part of the manufacturing, processing, refining, or~~
36 ~~fabricating process, or that constitute a research or storage facility~~
37 ~~used during the manufacturing process. Buildings used solely for~~
38 ~~warehousing purposes after completion of the manufacturing~~
39 ~~process are not included.~~

40 ~~(E) Fuels used or consumed in the manufacturing process.~~

1 ~~(F) Property used in recycling.~~

2 ~~(e) No exemption shall be allowed under this section unless the~~
3 ~~purchaser furnishes the retailer with an exemption certificate,~~
4 ~~completed in accordance with any instructions or regulations as~~
5 ~~the board may prescribe, and the retailer subsequently furnishes~~
6 ~~the board with a copy of the exemption certificate. The exemption~~
7 ~~certificate shall contain the sales price of the machinery or~~
8 ~~equipment that is exempt pursuant to subdivision (a).~~

9 ~~(d) Notwithstanding any provision of the Bradley Burns~~
10 ~~Uniform Local Sales and Use Tax Law (Part 1.5 (commencing~~
11 ~~with Section 7200)) or the Transactions and Use Tax Law (Part 1.6~~
12 ~~(commencing with Section 7251)), the exemption established by~~
13 ~~this section shall not apply with respect to any tax levied by a~~
14 ~~county, city, or district pursuant to, or in accordance with, either~~
15 ~~of those laws.~~

16 ~~(e) (1) Notwithstanding subdivision (a), the exemption~~
17 ~~provided by this section shall not apply to any sale or use of~~
18 ~~property which, within one year from the date of purchase, is either~~
19 ~~removed from California or converted from an exempt use under~~
20 ~~subdivision (a) to some other use not qualifying for the exemption.~~

21 ~~(2) Notwithstanding subdivision (a), on or after January 1,~~
22 ~~1995, the exemption established by this section shall not apply~~
23 ~~with respect to any tax levied pursuant to Sections 6051.2 and~~
24 ~~6201.2, or pursuant to Section 35 of Article XIII of the California~~
25 ~~Constitution.~~

26 ~~(f) If a purchaser certifies in writing to the seller that the~~
27 ~~property purchased without payment of the tax will be used in a~~
28 ~~manner entitling the seller to regard the gross receipts from the sale~~
29 ~~as exempt from the sales tax, and within one year from the date of~~
30 ~~purchase, the purchaser (1) removes that property outside~~
31 ~~California, (2) converts that property for use in a manner not~~
32 ~~qualifying for the exemption, or (3) uses that property in a manner~~
33 ~~not qualifying for the exemption, the purchaser shall be liable for~~
34 ~~payment of sales tax, with applicable interest, as if the purchaser~~
35 ~~were a retailer making a retail sale of the property at the time the~~
36 ~~property is so removed, converted, or used, and the sales price of~~
37 ~~the property to the purchaser shall be deemed the gross receipts~~
38 ~~from that retail sale.~~

1 ~~(g) (1) This section shall remain in effect until the date~~
2 ~~specified in paragraph (2), on which date this section shall cease~~
3 ~~to be operative, and as of that date is repealed.~~

4 ~~(2) (A) This section shall cease to be operative on January 1,~~
5 ~~2001, or on January 1 of the earliest year thereafter, if the total~~
6 ~~employment in this state, as determined by the Employment~~
7 ~~Development Department on the preceding January 1, does not~~
8 ~~exceed by 100,000 jobs the total employment in this state on~~
9 ~~January 1, 1994. The department shall report annually to the~~
10 ~~Legislature with respect to the determination required by the~~
11 ~~preceding sentence.~~

12 ~~(B) For purposes of this paragraph, "total employment" means~~
13 ~~the total employment in the manufacturing sector, excluding~~
14 ~~employment in the aerospace sector.~~

15 ~~(h) This section applies to leases of tangible personal property~~
16 ~~classified as "continuing sales" and "continuing purchases" in~~
17 ~~accordance with Sections 6006.1 and 6010.1. The exemption~~
18 ~~established by this section shall apply to the rentals payable~~
19 ~~pursuant to such a lease, provided the lessee is a qualified person~~
20 ~~and the property is used in an activity described in subdivision (a).~~
21 ~~Rentals which meet the foregoing requirements are eligible for the~~
22 ~~exemption for a period of six years from the date of~~
23 ~~commencement of the lease. At the close of the six year period~~
24 ~~from the date of commencement of the lease, lease receipts are~~
25 ~~subject to tax without exemption.~~

26 ~~SEC. 3.—~~

27 *SEC. 2.* Section 17039 of the Revenue and Taxation Code is
28 amended to read:

29 17039. (a) Notwithstanding any provision in this part to the
30 contrary, for the purposes of computing tax credits, the term "net
31 tax" means the tax imposed under either Section 17041 or 17048
32 plus the tax imposed under Section 17504 (relating to lump-sum
33 distributions) less the credits allowed by Section 17054 (relating
34 to personal exemption credits) and any amount imposed under
35 paragraph (1) of subdivision (d) and paragraph (1) of subdivision
36 (e) of Section 17560. Notwithstanding the preceding sentence, the
37 "net tax" shall not be less than the tax imposed under Section
38 17504 (relating to the separate tax on lump-sum distributions), if
39 any. Credits shall be allowed against "net tax" in the following
40 order:

1 (1) Credits that do not contain carryover or refundable
2 provisions, except those described in paragraphs (4) and (5).

3 (2) Credits that contain carryover provisions but do not contain
4 refundable provisions, except for those that are allowed to reduce
5 “net tax” below the tentative minimum tax, as defined by Section
6 17062.

7 (3) Credits that contain both carryover and refundable
8 provisions.

9 (4) The minimum tax credit allowed by Section 17063 (relating
10 to the alternative minimum tax).

11 (5) Credits that are allowed to reduce “net tax” below the
12 tentative minimum tax, as defined by Section 17062.

13 (6) Credits for taxes paid to other states allowed by Chapter 12
14 (commencing with Section 18001).

15 (7) Credits that contain refundable provisions but do not
16 contain carryover provisions.

17 The order within each paragraph shall be determined by the
18 Franchise Tax Board.

19 (b) Notwithstanding the provisions of Sections 17061 (relating
20 to refunds pursuant to the Unemployment Insurance Code) and
21 19002 (relating to tax withholding), the credits provided in those
22 sections shall be allowed in the order provided in paragraph (6) of
23 subdivision (a).

24 (c) (1) Notwithstanding any other provision of this part, no tax
25 credit shall reduce the tax imposed under Section 17041 or 17048
26 plus the tax imposed under Section 17504 (relating to the separate
27 tax on lump-sum distributions) below the tentative minimum tax,
28 as defined by Section 17062, except the following credits:

29 (A) The credit allowed by Section 17052.2 (relating to teacher
30 retention tax credit).

31 (B) The credit allowed by former Section 17052.4 (relating to
32 solar energy).

33 (C) The credit allowed by former Section 17052.5 (relating to
34 solar energy, repealed on January 1, 1987).

35 (D) The credit allowed by former Section 17052.5 (relating to
36 solar energy, repealed on December 1, 1994).

37 (E) The credit allowed by Section 17052.12 (relating to
38 research expenses).

39 (F) The credit allowed by former Section 17052.13 (relating to
40 sales and use tax credit).

1 (G) The credit allowed by former Section 17052.15 (relating to
2 Los Angeles Revitalization Zone sales tax credit).

3 (H) The credit allowed by Section 17052.25 (relating to the
4 adoption costs credit).

5 (I) The credit allowed by Section 17053.5 (relating to the
6 renter's credit).

7 (J) The credit allowed by former Section 17053.8 (relating to
8 enterprise zone hiring credit).

9 (K) The credit allowed by former Section 17053.10 (relating to
10 Los Angeles Revitalization Zone hiring credit).

11 (L) The credit allowed by former Section 17053.11 (relating to
12 program area hiring credit).

13 (M) For each taxable year beginning on or after January 1,
14 1994, the credit allowed by former Section 17053.17 (relating to
15 Los Angeles Revitalization Zone hiring credit).

16 (N) The credit allowed by Section 17053.33 (relating to
17 targeted tax area sales or use tax credit).

18 (O) The credit allowed by Section 17053.34 (relating to
19 targeted tax area hiring credit).

20 (P) The credit allowed by Section 17053.49 (relating to
21 qualified property).

22 (Q) The credit allowed by Section 17053.51 (relating to career
23 technical education campaign).

24 (R) The credit allowed by Section 17053.70 (relating to
25 enterprise zone sales or use tax credit).

26 (S) The credit allowed by Section 17053.74 (relating to
27 enterprise zone hiring credit).

28 (T) The credit allowed by Section 17054 (relating to credits for
29 personal exemption).

30 (U) The credit allowed by Section 17054.5 (relating to the
31 credits for a qualified joint custody head of household and a
32 qualified taxpayer with a dependent parent).

33 (V) The credit allowed by Section 17054.7 (relating to the
34 credit for a senior head of household).

35 (W) The credit allowed by former Section 17057 (relating to
36 clinical testing expenses).

37 (X) The credit allowed by Section 17058 (relating to
38 low-income housing).

39 (Y) The credit allowed by Section 17061 (relating to refunds
40 pursuant to the Unemployment Insurance Code).

1 (Z) Credits for taxes paid to other states allowed by Chapter 12
2 (commencing with Section 18001).

3 (AA) The credit allowed by Section 19002 (relating to tax
4 withholding).

5 (2) Any credit that is partially or totally denied under paragraph
6 (1) shall be allowed to be carried over and applied to the net tax in
7 succeeding taxable years, if the provisions relating to that credit
8 include a provision to allow a carryover when that credit exceeds
9 the net tax.

10 (d) Unless otherwise provided, any remaining carryover of a
11 credit allowed by a section that has been repealed or made
12 inoperative shall continue to be allowed to be carried over under
13 the provisions of that section as it read immediately prior to being
14 repealed or becoming inoperative.

15 (e) (1) Unless otherwise provided, if two or more taxpayers
16 (other than husband and wife) share in costs that would be eligible
17 for a tax credit allowed under this part, each taxpayer shall be
18 eligible to receive the tax credit in proportion to his or her
19 respective share of the costs paid or incurred.

20 (2) In the case of a partnership, the credit shall be allocated
21 among the partners pursuant to a written partnership agreement in
22 accordance with Section 704 of the Internal Revenue Code,
23 relating to partner's distributive share.

24 (3) In the case of a husband and wife who file separate returns,
25 the credit may be taken by either or equally divided between them.

26 (f) Unless otherwise provided, in the case of a partnership, any
27 credit allowed by this part shall be computed at the partnership
28 level, and any limitation on the expenses qualifying for the credit
29 or limitation upon the amount of the credit shall be applied to the
30 partnership and to each partner.

31 (g) (1) With respect to any taxpayer that directly or indirectly
32 owns an interest in a business entity that is disregarded for tax
33 purposes pursuant to Section 23038 and any regulations
34 thereunder, the amount of any credit or credit carryforward
35 allowable for any taxable year attributable to the disregarded
36 business entity shall be limited in accordance with paragraphs (2)
37 and (3).

38 (2) The amount of any credit otherwise allowed under this part,
39 including any credit carryover from prior years, that may be
40 applied to reduce the taxpayer's "net tax," as defined in

subdivision (a), for the taxable year shall be limited to an amount equal to the excess of the taxpayer's regular tax (as defined in Section 17062), determined by including income attributable to the disregarded business entity that generated the credit or credit carryover, over the taxpayer's regular tax (as defined in Section 17062), determined by excluding the income attributable to that disregarded business entity. No credit shall be allowed if the taxpayer's regular tax (as defined in Section 17062), determined by including the income attributable to the disregarded business entity, is less than the taxpayer's regular tax (as defined in Section 17062), determined by excluding the income attributable to the disregarded business entity.

(3) If the amount of a credit allowed pursuant to the section establishing the credit exceeds the amount allowable under this subdivision in any taxable year, the excess amount may be carried over to subsequent taxable years pursuant to subdivisions (c) and (d).

(h) (1) Unless otherwise specifically provided, in the case of a taxpayer that is a partner or shareholder of an eligible pass-through entity described in paragraph (2), any credit passed through to the taxpayer in the taxpayer's first taxable year beginning on or after the date the credit is no longer operative may be claimed by the taxpayer in that taxable year, notwithstanding the repeal of the statute authorizing the credit prior to the close of that taxable year.

(2) For purposes of this subdivision, "eligible pass-through entity" means any partnership or S corporation that files its return on a fiscal year basis pursuant to Section 18566, and that is entitled to a credit pursuant to this part for the taxable year that begins during the last year the credit is operative.

(3) This subdivision shall apply to credits that become inoperative on or after the operative date of the act adding this subdivision.

~~SEC. 4. Section 17053.49 of the Revenue and Taxation Code is amended to read:~~

~~17053.49. (a) (1) A qualified taxpayer shall be allowed a credit against the "net tax," as defined in Section 17039, equal to the applicable percentage of the qualified cost of qualified property that is placed in service in this state. For purposes of this subdivision, the applicable percentage is:~~

~~(A) Six percent for property placed in service before January 1, 2005.~~

~~(B) Five percent for property placed in service on or after January 1, 2005, and before January 1, 2006.~~

~~(C) Four percent for property placed in service on or after January 1, 2006, and before January 1, 2007.~~

~~(D) Three percent for property placed in service on or after January 1, 2007, and before January 1, 2008.~~

~~(E) Two percent for property placed in service on or after January 1, 2008, and before January 1, 2009.~~

~~(F) One percent for property placed in service on or after January 1, 2009, and before January 1, 2010.~~

~~(2) In the case of any qualified costs paid or incurred on or after January 1, 1994, and prior to the first taxable year of the qualified taxpayer beginning on or after January 1, 1995, the credit provided under paragraph (1) shall be claimed by the qualified taxpayer on the qualified taxpayer's return for the first taxable year beginning on or after January 1, 1995. No credit shall be claimed under this section on a return filed for any taxable year commencing prior to the qualified taxpayer's first taxable year beginning on or after January 1, 1995.~~

~~(b) (1) For purposes of this section, "qualified cost" means any cost that satisfies each of the following conditions:~~

~~(A) Except as otherwise provided in this subparagraph, is a cost paid or incurred by the qualified taxpayer for the construction, reconstruction, or acquisition of qualified property on or after January 1, 1994, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i). In the case of any qualified property constructed, reconstructed, or acquired by the qualified taxpayer (or any person related to the qualified taxpayer within the meaning of Section 267 or 707 of the Internal Revenue Code) pursuant to a binding contract in existence on or prior to January 1, 1994, costs paid pursuant to that contract shall be subject to allocation as follows: contract costs shall be allocated to qualified property based on a ratio of costs actually paid prior to January 1, 1994, and total contract costs actually paid. "Cost paid" shall include, without limitation, contractual deposits and option payments. To the extent of costs allocated, whether or not currently deductible or depreciable for tax purposes, to a period prior to~~

1 ~~January 1, 1994, the cost shall be deemed allocated to property~~
2 ~~acquired before January 1, 1994, and is thus not a “qualified cost.”~~

3 ~~(B) Except as provided in paragraph (3) of subdivision (d) and~~
4 ~~subparagraph (B) of paragraph (4) of subdivision (d), is an amount~~
5 ~~upon which the qualified taxpayer has paid, directly or indirectly,~~
6 ~~as a separately stated contract amount or as determined from the~~
7 ~~records of the qualified taxpayer, sales or use tax under Part 1~~
8 ~~(commencing with Section 6001).~~

9 ~~(C) Is an amount properly chargeable to the capital account of~~
10 ~~the qualified taxpayer.~~

11 ~~(2) (A) For purposes of this subdivision, any contract entered~~
12 ~~into on or after January 1, 1994, that is a successor or replacement~~
13 ~~contract to a contract that was binding prior to January 1, 1994,~~
14 ~~shall be treated as a binding contract in existence prior to January~~
15 ~~1, 1994.~~

16 ~~(B) If a successor or replacement contract is entered into on or~~
17 ~~after January 1, 1994, and the subject of the successor or~~
18 ~~replacement contract relates both to amounts for the construction,~~
19 ~~reconstruction, or acquisition of qualified property described in~~
20 ~~the original binding contract and to costs for the construction,~~
21 ~~reconstruction, or acquisition of qualified property not described~~
22 ~~in the original binding contract, then the portion of those amounts~~
23 ~~described in the successor or replacement contract that were not~~
24 ~~described in the original binding contract shall not be treated as~~
25 ~~costs paid or incurred pursuant to a binding contract in existence~~
26 ~~on or prior to January 1, 1994, under subparagraph (A) of~~
27 ~~paragraph (1).~~

28 ~~(3) (A) For purposes of this section, an option contract in~~
29 ~~existence prior to January 1, 1994, under which a qualified~~
30 ~~taxpayer (or any other person related to the qualified taxpayer~~
31 ~~within the meaning of Section 267 or 707 of the Internal Revenue~~
32 ~~Code) had an option to acquire qualified property, shall be treated~~
33 ~~as a binding contract under the rules in paragraph (2). For purposes~~
34 ~~of this subparagraph, an option contract shall not include an option~~
35 ~~under which the optionholder will forfeit an amount less than 10~~
36 ~~percent of the fixed option price in the event the option is not~~
37 ~~exercised.~~

38 ~~(B) For purposes of this section, a contract shall be treated as~~
39 ~~binding even if the contract is subject to a condition.~~

~~(4) For purposes of this subdivision, in the case of any qualified taxpayer engaged in those lines of business described in Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, “the first taxable year beginning on or after January 1, 1998,” shall be substituted for “January 1, 1994,” in each place in which it appears.~~

~~(c) (1) For purposes of this section, “qualified taxpayer” means any taxpayer engaged in those lines of business described in Codes 2011 to 3999, inclusive, or Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition.~~

~~(2) In the case of any passthrough entity, the determination of whether a taxpayer is a qualified taxpayer under this section shall be made at the entity level and any credit under this section or Section 23649 shall be allowed to the passthrough entity and passed through to the partners or shareholders in accordance with applicable provisions of Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001). For purposes of this paragraph, the term “passthrough entity” means any partnership or S corporation.~~

~~(3) The Franchise Tax Board may prescribe regulations to carry out the purposes of this section, including any regulations necessary to prevent the avoidance of the effect of this section through splitups, shell corporations, partnerships, tiered ownership structures, sale-leaseback transactions, or otherwise.~~

~~(d) For purposes of this section, “qualified property” means property that is described as any of the following:~~

~~(1) Tangible personal property that is defined in Section 1245(a) of the Internal Revenue Code for use by a qualified taxpayer in those lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, that is primarily used for any of the following:~~

~~(A) For the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the process and ending at the point at which the~~

1 ~~manufacturing, processing, refining, fabricating, or recycling has~~
2 ~~altered tangible personal property to its completed form, including~~
3 ~~packaging, if required.~~

4 ~~(B) In research and development.~~

5 ~~(C) To maintain, repair, measure, or test any property described~~
6 ~~in this paragraph.~~

7 ~~(D) For pollution control that meets or exceeds standards~~
8 ~~established by the state or by any local or regional governmental~~
9 ~~agency within the state.~~

10 ~~(E) For recycling.~~

11 ~~(2) Computers and computer peripheral equipment, as defined~~
12 ~~in Section 168(i)(2)(B) of the Internal Revenue Code, that is~~
13 ~~tangible personal property as defined in Section 1245(a) of the~~
14 ~~Internal Revenue Code for use by a qualified taxpayer in those~~
15 ~~lines of business described in SIC Codes 7371 to 7373, inclusive,~~
16 ~~of the SIC Manual, 1987 edition, that is primarily used to develop~~
17 ~~or manufacture prepackaged software or custom software~~
18 ~~prepared to the special order of the purchaser who uses the~~
19 ~~program to produce and sell or license copies of the program as~~
20 ~~prepackaged software.~~

21 ~~(3) The value of any capitalized labor costs that are directly~~
22 ~~allocable to the construction or modification of property described~~
23 ~~in paragraph (1) or (2).~~

24 ~~(4) In the case of any qualified taxpayer engaged in~~
25 ~~manufacturing activities described in SIC Code 357 or 367, those~~
26 ~~activities related to biotechnology described in SIC Code 8731,~~
27 ~~those activities related to biopharmaceutical establishments only~~
28 ~~that are described in SIC Codes 2833 to 2836, inclusive, those~~
29 ~~activities related to space vehicles and parts described in SIC~~
30 ~~Codes 3761 to 3769, inclusive, those activities related to space~~
31 ~~satellites and communications satellites and equipment described~~
32 ~~in SIC Codes 3663 and 3812 (but only with respect to “qualified~~
33 ~~property” that is placed in service on or after January 1, 1996), or~~
34 ~~those activities related to semiconductor equipment~~
35 ~~manufacturing described in SIC Code 3559 (but only with respect~~
36 ~~to “qualified property” that is placed in service on or after January~~
37 ~~1, 1997), “qualified property” also includes the following:~~

38 ~~(A) Special purpose buildings and foundations that are~~
39 ~~constructed or modified for use by the qualified taxpayer primarily~~
40 ~~in a manufacturing, processing, refining, or fabricating process, or~~

1 as a research or storage facility primarily used in connection with
2 a manufacturing process.

3 (B) The value of any capitalized labor costs that are directly
4 allocable to the construction or modification of special purpose
5 buildings and foundations that are used primarily in the
6 manufacturing, processing, refining, or fabricating process, or as
7 a research or storage facility primarily used in connection with a
8 manufacturing process.

9 (C) (i) For purposes of this paragraph, “special purpose
10 building and foundation” means only a building and the
11 foundation immediately underlying the building that is
12 specifically designed and constructed or reconstructed for the
13 installation, operation, and use of specific machinery and
14 equipment with a special purpose, which machinery and
15 equipment, after installation, will become affixed to or a fixture of
16 the real property, and the construction or reconstruction of which
17 is specifically designed and used exclusively for the specified
18 purposes as set forth in subparagraph (A) (“qualified purpose”).

19 (ii) A building is specifically designed and constructed or
20 modified for a qualified purpose if it is not economical to design
21 and construct the building for the intended purpose and then use
22 the structure for a different purpose.

23 (iii) For purposes of clause (i) and clause (vi), a building is used
24 exclusively for a qualified purpose only if its use does not include
25 a use for which it was not specifically designed and constructed or
26 modified. Incidental use of a building for nonqualified purposes
27 does not preclude the building from being a special purpose
28 building. “Incidental use” means a use which is both related and
29 subordinate to the qualified purpose. It will be conclusively
30 presumed that a use is not subordinate if more than one third of the
31 total usable volume of the building is devoted to a use which is not
32 a qualified purpose.

33 (iv) In the event an entire building does not qualify as a special
34 purpose building, a taxpayer may establish that a portion of a
35 building, and the foundation immediately underlying the portion,
36 qualifies for treatment as a special purpose building and
37 foundation if the portion satisfies all of the definitional provisions
38 in this subparagraph.

39 (v) To the extent that a building is not a special purpose
40 building as defined above, but a portion of the building qualifies

1 for treatment as a special purpose building, then all equipment
2 which exclusively supports the qualified purpose occurring within
3 that portion and which would qualify as Internal Revenue Code
4 Section 1245 property if it were not a fixture or affixed to the
5 building shall be treated as a cost of the portion of the building
6 which qualifies for treatment as a special purpose building.

7 (vi) Buildings and foundations which do not meet the
8 definition of a special purpose building and foundation set forth
9 above include, but are not limited to: buildings designed and
10 constructed or reconstructed principally to function as a general
11 purpose manufacturing, industrial, or commercial building;
12 research facilities that are used primarily prior to or after, or prior
13 to and after, the manufacturing process; or storage facilities that
14 are used primarily prior to or after, or prior to and after, completion
15 of the manufacturing process. A research facility shall not be
16 considered to be used primarily prior to or after, or prior to and
17 after, the manufacturing process if its purpose and use relate
18 exclusively to the development and regulatory approval of the
19 manufacturing process for specific biopharmaceutical products. A
20 research facility which is used primarily in connection with the
21 discovery of an organism from which a biopharmaceutical product
22 or process is developed does not meet the requirements of the
23 preceding sentence.

24 (5) Subject to the provisions in subparagraph (B) of paragraph
25 (1) of subdivision (b), qualified property also includes computer
26 software that is primarily used for those purposes set forth in
27 paragraph (1) or (2) of this subdivision.

28 (6) Qualified property does not include any of the following:

29 (A) Furniture.

30 (B) Facilities used for warehousing purposes after completion
31 of the manufacturing process.

32 (C) Inventory.

33 (D) Equipment used in the extraction process.

34 (E) Equipment used to store finished products that have
35 completed the manufacturing process.

36 (F) Any tangible personal property that is used in
37 administration, general management, or marketing.

38 (G) Any vehicle for which a credit is claimed pursuant to
39 Section 17052.11 or 23603.

40 (e) For purposes of this section:

~~(1) “Biopharmaceutical activities” means those activities that use organisms or materials derived from organisms, and their cellular, subcellular, or molecular components, in order to provide pharmaceutical products for human or animal therapeutics and diagnostics. Biopharmaceutical activities make use of living organisms to make commercial products, as opposed to pharmaceutical activities which make use of chemical compounds to produce commercial products.~~

~~(2) “Fabricating” means to make, build, create, produce, or assemble components or property to work in a new or different manner.~~

~~(3) “Manufacturing” means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.~~

~~(4) “Other biotechnology activities” means activities consisting of the application of recombinant DNA technology to produce commercial products, as well as activities regarding pharmaceutical delivery systems designed to provide a measure of control over the rate, duration, and site of pharmaceutical delivery.~~

~~(5) “Primarily” means tangible personal property used 50 percent or more of the time in an activity described in subdivision (d).~~

~~(6) “Process” means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer’s manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified taxpayer’s manufacturing, processing, refining, fabricating, or recycling activity is~~

1 conducted, shall not be considered to have been introduced into the
2 manufacturing, processing, refining, fabricating, or recycling
3 process.

4 (7) “Processing” means the physical application of the
5 materials and labor necessary to modify or change the
6 characteristics of property.

7 (8) “Refining” means the process of converting a natural
8 resource to an intermediate or finished product.

9 (9) “Research and development” means those activities that
10 are described in Section 174 of the Internal Revenue Code or in any
11 regulations thereunder.

12 (10) “Small business” means a qualified taxpayer that meets
13 any of the following requirements during the taxable year for
14 which the credit is allowed:

15 (A) Has gross receipts of less than fifty million dollars
16 (\$50,000,000).

17 (B) Has net assets of less than fifty million dollars
18 (\$50,000,000).

19 (C) Has a total credit of less than one million dollars
20 (\$1,000,000).

21 (D) For taxable years beginning on or after January 1, 1997, is
22 engaged in biopharmaceutical activities or other biotechnology
23 activities that are described in Codes 2833 to 2836, inclusive, of
24 the Standard Industrial Classification (SIC) Manual published by
25 the United States Office of Management and Budget, 1987 edition,
26 and has not received regulatory approval for any product from the
27 United States Food and Drug Administration.

28 (f) The credit allowed under subdivision (a) shall apply to
29 qualified property that is acquired by or subject to lease by a
30 qualified taxpayer, subject to the following special rules:

31 (1) A lessor of qualified property, irrespective of whether the
32 lessor is a qualified taxpayer, shall not be allowed the credit
33 provided under subdivision (a) with respect to any qualified
34 property leased to another qualified taxpayer.

35 (2) For purposes of paragraphs (2) and (3) of subdivision (b),
36 “binding contract” shall include any lease agreement with respect
37 to the qualified property.

38 (3) (A) For purposes of determining the qualified cost paid or
39 incurred by a lessee in any leasing transaction that is not treated as

1 a sale under Part 1 (commencing with Section 6001), the following
2 rules shall apply:

3 (i) ~~Except as provided by subparagraph (C) of this paragraph,~~
4 ~~subparagraphs (A) and (C) of paragraph (1) of subdivision (b)~~
5 ~~shall not apply.~~

6 (ii) ~~Except as provided in subparagraph (B) and clause (iii), the~~
7 ~~“qualified cost” upon which the lessee shall compute the credit~~
8 ~~provided under this section shall be equal to the original cost to the~~
9 ~~lessor (within the meaning of Section 18031) of the qualified~~
10 ~~property that is the subject of the lease.~~

11 (iii) ~~Except as provided in clause (iv), the requirement of~~
12 ~~subparagraph (B) of paragraph (1) of subdivision (b) shall be~~
13 ~~treated as satisfied only if the lessor has made a timely election~~
14 ~~under either Section 6094.1 or subdivision (d) of Section 6244 and~~
15 ~~has paid sales tax reimbursement or use tax measured by the~~
16 ~~purchase price of the qualified property (within the meaning of~~
17 ~~paragraph (5) of subdivision (g) of Section 6006). For purposes of~~
18 ~~this subdivision and clause (iv), the amount of original cost to the~~
19 ~~lessor which may be taken into account under clause (ii) shall not~~
20 ~~exceed the purchase price upon which sales tax reimbursement or~~
21 ~~use tax has been paid under the preceding sentence or under clause~~
22 ~~(iv).~~

23 (iv) ~~With respect to leases entered into between January 1,~~
24 ~~1994, and the effective date of this clause, the lessor may elect to~~
25 ~~pay use tax measured by the purchase price of the property by~~
26 ~~reporting and paying the tax with the return of the lessor for the~~
27 ~~fourth calendar quarter of 1994. In computing the use tax under the~~
28 ~~preceding sentence, a credit shall be allowed under Part 1~~
29 ~~(commencing with Section 6001) for all sales or use tax previously~~
30 ~~paid on the lease.~~

31 (B) ~~For purposes of applying subparagraph (A) only, the~~
32 ~~following special rules shall apply:~~

33 (i) ~~The original cost to the lessor of the qualified property shall~~
34 ~~be reduced by the amount of any original cost of that property that~~
35 ~~was taken into account by any predecessor lessee in computing the~~
36 ~~credit allowable under this section.~~

37 (ii) ~~Clause (i) shall not apply in any case where the predecessor~~
38 ~~lessee was required to recapture the credit provided under this~~
39 ~~section pursuant to subdivision (g).~~

~~(iii) For purposes of this section only, in any case where a successor lessor has acquired qualified property from a predecessor lessor in a transaction not treated as a sale under Part 1 (commencing with Section 6001), the original cost to the successor lessor of the qualified property shall be reduced by the amount of the original cost of the qualified property that was taken into account by any lessee of the predecessor lessor in computing the credit allowable under this section.~~

~~(C) In determining the original cost of any qualified property under this paragraph, only amounts paid or incurred by the lessor on or after January 1, 1994, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i), shall be taken into account. In the case of any qualified property constructed, reconstructed, or acquired by a lessor pursuant to a binding contract in existence on or prior to January 1, 1994, the allocation rule specified in subparagraph (A) of paragraph (1) of subdivision (b) shall apply in determining the original cost to the lessor of qualified property.~~

~~(D) Notwithstanding subparagraph (A), in the case of any leasing transaction for which the lessee is allowed the credit under this section and thereafter the lessee (or any party related to the lessee within the meaning of Section 267 or 318 of the Internal Revenue Code) acquires the qualified property from the lessor (or any successor lessor) within one year from the date the qualified property is first used by the lessee under the terms of the lease, the lessee's (or related party's) acquisition of the qualified property from the lessor (or successor lessor) shall be treated as a disposition by the lessee of the qualified property that was subject to the lease under subdivision (g).~~

~~(4) For purposes of determining the qualified cost paid or incurred by a lessee in any leasing transaction that is treated as a sale under Part 1 (commencing with Section 6001), the following rules shall apply:~~

~~(A) Subparagraph (A) of paragraph (1) of subdivision (b) shall be applied by substituting the term "purchase" for the term "construction, reconstruction, or acquisition."~~

~~(B) Subparagraph (C) of paragraph (1) of subdivision (b) shall apply.~~

~~(C) The requirement of subparagraph (B) of paragraph (1) of subdivision (b) shall be treated as satisfied at the time that either~~

~~the lessor or the qualified taxpayer pays sales or use tax under Part 1 (commencing with Section 6001).~~

~~(5) (A) In the case of any leasing transaction described in paragraph (3), the lessor shall provide a statement to the lessee specifying the amount of the lessor's original cost of the qualified property and the amount of that cost upon which a sales or use tax was paid within 45 days after the close of the lessee's taxable year in which the credit is allowable to the lessee under this section.~~

~~(B) The statement required under subparagraph (A) shall be made available to the Franchise Tax Board upon request.~~

~~(6) For purposes of this subdivision, in the case of any qualified taxpayer engaged in those lines of business described in Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, "the first taxable year beginning on or after January 1, 1998," shall be substituted for "January 1, 1994," in each place in which it appears. In addition, "the effective date of this paragraph" shall be substituted for "the effective date of this clause" and "fourth calendar quarter of 1998" shall be substituted for "fourth calendar quarter of 1994."~~

~~(g) No credit shall be allowed if the qualified property is removed from the state, is disposed of to an unrelated party, or is used for any purpose not qualifying for the credit provided in this section in the same taxable year in which the qualified property is first placed in service in this state. If any qualified property for which a credit is allowed pursuant to this section is thereafter removed from this state, disposed of to an unrelated party, or used for any purpose not qualifying for the credit provided in this section within one year from the date the qualified property is first placed in service in this state, the amount of the credit allowed by this section for that qualified property shall be recaptured by adding that credit amount to the net tax of the qualified taxpayer for the taxable year in which the qualified property is disposed of, removed, or put to an ineligible use.~~

~~(h) In the case where the credit allowed by this section exceeds the "net tax," the excess may be carried over to reduce the "net tax" in the following year, and succeeding years as follows:~~

~~(1) Except as provided in paragraph (2), for the seven succeeding years if necessary, until the credit is exhausted.~~

~~(2) In the case of a small business, for the nine succeeding years, if necessary, until the credit is exhausted.~~

~~(i) (1) This section shall remain in effect until the date specified in paragraph (2), on which date this section shall cease to be operative, and as of that date is repealed.~~

~~(2) This section shall cease to be operative on January 1, 2011.~~

~~(j) The amendments made by Chapter 954 of the Statutes of 1996 shall be operative for taxable years beginning on or after January 1, 1997, except as provided in paragraph (3) of subdivision (d).~~

~~(k) The amendments made by Chapter 323 of the Statutes of 1998 shall be operative for taxable years beginning on or after January 1, 1998.~~

~~SEC. 5.—~~

SEC. 3. Section 17053.51 is added to the Revenue and Taxation Code, to read:

17053.51. (a) A qualified taxpayer shall be allowed a credit against the “net tax,” as defined in Section 17039, in an amount equal to the applicable percentage of the qualified cost of qualified property that is placed in service in this state. For purposes of this subdivision, the applicable percentage is:

~~(1) Two One percent for property placed in service on or after January 1, 2005, and before January 1, 2006.~~

~~(2) Three percent for property placed in service on or after January 1, 2006, and before January 1, 2007.~~

~~(3) Four percent for property placed in service on or after January 1, 2007, and before January 1, 2008.~~

~~(4) Five percent for property placed in service on or after January 1, 2008, and before January 1, 2009.~~

~~(5) Six percent for property placed in service on or after January 1, 2009, and before January 1, 2010.~~

~~(6) January 1, 2007, and before January 1, 2009.~~

~~(2) Four percent for property placed in service on or after January 1, 2009, and before January 1, 2010.~~

~~(3) Seven percent for property placed in service on or after January 1, 2010.~~

(b) (1) For purposes of this section, “qualified cost” means any cost that satisfies each of the following conditions:

(A) Except as otherwise provided in this subparagraph, is a cost paid or incurred by the qualified taxpayer for the construction,

1 reconstruction, or acquisition of qualified property on or after
2 January 1, ~~2005~~ 2007, and prior to the date this section ceases to
3 be operative under paragraph (2) of subdivision (i). In the case of
4 any qualified property constructed, reconstructed, or acquired by
5 the qualified taxpayer (or any person related to the qualified
6 taxpayer within the meaning of Section 267 or 707 of the Internal
7 Revenue Code) pursuant to a binding contract in existence on or
8 prior to January 1, ~~2005~~ 2007, costs paid pursuant to that contract
9 shall be subject to allocation as follows: contract costs shall be
10 allocated to qualified property based on a ratio of costs actually
11 paid prior to January 1, ~~2005~~ 2007, and total contract costs
12 actually paid. "Cost paid" shall include, without limitation,
13 contractual deposits, and option payments. To the extent of costs
14 allocated, whether or not currently deductible or depreciable for
15 tax purposes, to a period prior to January 1, ~~2005~~ 2007, the cost
16 shall be deemed allocated to property acquired before January 1,
17 ~~2005~~ 2007, and is thus not a "qualified cost."

18 (B) Except as provided in paragraph (3) of subdivision (d) and
19 subparagraph (B) of paragraph (4) of subdivision (d), is an amount
20 upon which the qualified taxpayer has paid, directly or indirectly
21 as a separately stated contract amount or as determined from the
22 records of the qualified taxpayer, sales or use tax under Part 1
23 (commencing with Section 6001).

24 (C) Is an amount properly chargeable to the capital account of
25 the qualified taxpayer.

26 (2) (A) For purposes of this subdivision, any contract entered
27 into on or after January 1, ~~2005~~ 2007, that is a successor or
28 replacement contract to a contract that was binding prior to
29 January 1, ~~2005~~ 2007, shall be treated as a binding contract in
30 existence prior to January 1, ~~2005~~ 2007.

31 (B) If a successor or replacement contract is entered into on or
32 after January 1, ~~2005~~ 2007, and the subject of the successor or
33 replacement contract relates both to amounts for the construction,
34 reconstruction, or acquisition of qualified property described in
35 the original binding contract and to costs for the construction,
36 reconstruction, or acquisition of qualified property not described
37 in the original binding contract, then the portion of those amounts
38 described in the successor or replacement contract that were not
39 described in the original binding contract shall not be treated as
40 costs paid or incurred pursuant to a binding contract in existence

1 on or prior to January 1, ~~2005~~ 2007, under subparagraph (A) of
2 paragraph (1).

3 (3) (A) For purposes of this section, an option contract in
4 existence prior to January 1, ~~2005~~ 2007, under which a qualified
5 taxpayer (or any other person related to the qualified taxpayer
6 within the meaning of Section 267 or 707 of the Internal Revenue
7 Code) had an option to acquire qualified property, shall be treated
8 as a binding contract under the rules in paragraph (2). For purposes
9 of this subparagraph, an option contract shall not include an option
10 under which the optionholder will forfeit an amount less than 10
11 percent of the fixed option price in the event the option is not
12 exercised.

13 (B) For purposes of this section, a contract shall be treated as
14 binding even if the contract is subject to a condition.

15 (c) (1) For purposes of this section, “qualified taxpayer”
16 means any taxpayer that is both of the following:

17 (A) Engaged in those lines of business described in Codes 2011
18 to 3999, inclusive, or Codes 7371 to 7373, inclusive, of the
19 Standard Industrial Classification (SIC) Manual published by the
20 United States Office of Management and Budget, 1987 edition.

21 (B) Certified, in the form and manner prescribed by the State
22 Department of Education, as a qualified participant in the Career
23 Technical Education Campaign pursuant to Section 52337 of the
24 Education Code for the taxable year for which a credit is claimed
25 under this section.

26 (2) In the case of any passthrough entity, the determination of
27 whether a taxpayer is a qualified taxpayer shall be made at the
28 entity level and any credit under this section or Section 23651 shall
29 be allowed to the passthrough entity and passed through to the
30 partners or shareholders in accordance with applicable provisions
31 of this part or Part 11 (commencing with Section 23001). For
32 purposes of this paragraph, the term “passthrough entity” means
33 any partnership or S corporation.

34 (3) The Franchise Tax Board may prescribe regulations to carry
35 out the purposes of this section, including any regulations
36 necessary to prevent the avoidance of the effect of this section
37 through splitups, shell corporations, partnerships, tiered
38 ownership structures, sale-leaseback transactions, or otherwise.

39 (d) For purposes of this section, “qualified property” means
40 property that is described as any of the following:

(1) Tangible personal property that is defined in Section 1245(a) of the Internal Revenue Code for use by a qualified taxpayer in those lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, that is primarily used for any of the following:

(A) For the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the process and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling has altered tangible personal property to its completed form, including packaging, if required.

(B) In research and development.

(C) To maintain, repair, measure, or test any property described in this paragraph.

(D) For pollution control that meets or exceeds standards established by the state or by any local or regional governmental agency within the state.

(E) For recycling.

(2) Computers and computer peripheral equipment, as defined in Section 168(i)(2)(B) of the Internal Revenue Code, that is tangible personal property as defined in Section 1245(a) of the Internal Revenue Code for use by a qualified taxpayer in those lines of business described in SIC Codes 7371 to 7373, inclusive, of the SIC Manual, 1987 edition, that is primarily used to develop or manufacture prepackaged software or custom software prepared to the special order of the purchaser who uses the program to produce and sell or license copies of the program as prepackaged software.

(3) The value of any capitalized labor costs that are directly allocable to the construction or modification of property described in paragraph (1) or (2).

(4) In the case of any qualified taxpayer engaged in manufacturing activities described in SIC Code 357 or 367, those activities related to biotechnology described in SIC Code 8731, those activities related to biopharmaceutical establishments only that are described in SIC Codes 2833 to 2836, inclusive, those activities related to space vehicles and parts described in SIC

Codes 3761 to 3769, inclusive, those activities related to space satellites and communications satellites and equipment described in SIC Codes 3663 and 3812, or those activities related to semiconductor equipment manufacturing described in SIC Code 3559, “qualified property” also includes the following:

(A) Special purpose buildings and foundations that are constructed or modified for use by the qualified taxpayer primarily in a manufacturing, processing, refining, or fabricating process, or as a research or storage facility primarily used in connection with a manufacturing process.

(B) The value of any capitalized labor costs that are directly allocable to the construction or modification of special purpose buildings and foundations that are used primarily in the manufacturing, processing, refining, or fabricating process, or as a research or storage facility primarily used in connection with a manufacturing process.

(C) (i) For purposes of this paragraph, “special purpose building and foundation” means only a building and the foundation immediately underlying the building that is specifically designed and constructed or reconstructed for the installation, operation, and use of specific machinery and equipment with a special purpose, which machinery and equipment, after installation, will become affixed to or a fixture of the real property, and the construction or reconstruction of which is specifically designed and used exclusively for the specified purposes as set forth in subparagraph (A).

(ii) A building is specifically designed and constructed or modified for a qualified purpose if it is not economical to design and construct the building for the intended purpose and then use the structure for a different purpose.

(iii) For purposes of clause (i) and clause (vi), a building is used exclusively for a qualified purpose only if its use does not include a use for which it was not specifically designed and constructed or modified. Incidental use of a building for nonqualified purposes does not preclude the building from being a special purpose building. “Incidental use” means a use which is both related and subordinate to the qualified purpose. It will be conclusively presumed that a use is not subordinate if more than one-third of the total usable volume of the building is devoted to a use which is not a qualified purpose.

(iv) In the event an entire building does not qualify as a special purpose building, a taxpayer may establish that a portion of a building, and the foundation immediately underlying the portion, qualifies for treatment as a special purpose building and foundation if the portion satisfies all of the definitional provisions in this subparagraph.

(v) To the extent that a building is not a special purpose building as defined above, but a portion of the building qualifies for treatment as a special purpose building, then all equipment which exclusively supports the qualified purpose occurring within that portion and which would qualify as Section 1245 of the Internal Revenue Code property if it were not a fixture or affixed to the building shall be treated as a cost of the portion of the building which qualifies for treatment as a special purpose building.

(vi) Buildings and foundations which do not meet the definition of a special purpose building and foundation set forth above include, but are not limited to: buildings designed and constructed or reconstructed principally to function as a general purpose manufacturing, industrial, or commercial building; research facilities that are used primarily prior to or after, or prior to and after, the manufacturing process; or storage facilities that are used primarily prior to or after, or prior to and after, completion of the manufacturing process. A research facility shall not be considered to be used primarily prior to or after, or prior to and after, the manufacturing process if its purpose and use relate exclusively to the development and regulatory approval of the manufacturing process for specific biopharmaceutical products. A research facility which is used primarily in connection with the discovery of an organism from which a biopharmaceutical product or process is developed does not meet the requirements of the preceding sentence.

(5) Subject to the provisions in subparagraph (B) of paragraph (1) of subdivision (b), qualified property also includes computer software that is primarily used for those purposes set forth in paragraph (1) or (2) of this subdivision.

(6) Qualified property does not include any of the following:

(A) Furniture.

(B) Facilities used for warehousing purposes after completion of the manufacturing process.

1 (C) Inventory.

2 (D) Equipment used in the extraction process.

3 (E) Equipment used to store finished products that have
4 completed the manufacturing process.

5 (F) Any tangible personal property that is used in
6 administration, general management, or marketing.

7 (e) For purposes of this section:

8 (1) “Biopharmaceutical activities” means those activities that
9 use organisms or materials derived from organisms, and their
10 cellular, subcellular, or molecular components, in order to provide
11 pharmaceutical products for human or animal therapeutics and
12 diagnostics. Biopharmaceutical activities make use of living
13 organisms to make commercial products, as opposed to
14 pharmaceutical activities which make use of chemical compounds
15 to produce commercial products.

16 (2) “Fabricating” means to make, build, create, produce, or
17 assemble components or property to work in a new or different
18 manner.

19 (3) “Manufacturing” means the activity of converting or
20 conditioning property by changing the form, composition, quality,
21 or character of the property for ultimate sale at retail or use in the
22 manufacturing of a product to be ultimately sold at retail.
23 Manufacturing includes any improvements to tangible personal
24 property that result in a greater service life or greater functionality
25 than that of the original property.

26 (4) “Other biotechnology activities” means activities
27 consisting of the application of recombinant DNA technology to
28 produce commercial products, as well as activities regarding
29 pharmaceutical delivery systems designed to provide a measure of
30 control over the rate, duration, and site of pharmaceutical delivery.

31 (5) “Primarily” means tangible personal property used 50
32 percent or more of the time in an activity described in subdivision
33 (d).

34 (6) “Process” means the period beginning at the point at which
35 any raw materials are received by the qualified taxpayer and
36 introduced into the manufacturing, processing, refining,
37 fabricating, or recycling activity of the qualified taxpayer and
38 ending at the point at which the manufacturing, processing,
39 refining, fabricating, or recycling activity of the qualified taxpayer
40 has altered tangible personal property to its completed form,

1 including packaging, if required. Raw materials shall be
2 considered to have been introduced into the process when the raw
3 materials are stored on the same premises where the qualified
4 taxpayer's manufacturing, processing, refining, fabricating, or
5 recycling activity is conducted. Raw materials that are stored on
6 premises other than where the qualified taxpayer's manufacturing,
7 processing, refining, fabricating, or recycling activity is
8 conducted, shall not be considered to have been introduced into the
9 manufacturing, processing, refining, fabricating, or recycling
10 process.

11 (7) "Processing" means the physical application of the
12 materials and labor necessary to modify or change the
13 characteristics of property.

14 (8) "Refining" means the process of converting a natural
15 resource to an intermediate or finished product.

16 (9) "Research and development" means those activities that
17 are described in Section 174 of the Internal Revenue Code or in any
18 regulations thereunder.

19 (10) "Small business" means a qualified taxpayer that meets
20 any of the following requirements during the income year for
21 which the credit is allowed:

22 (A) Has gross receipts of less than fifty million dollars
23 (\$50,000,000).

24 (B) Has net assets of less than fifty million dollars
25 (\$50,000,000).

26 (C) Has a total credit of less than one million dollars
27 (\$1,000,000).

28 (D) Is engaged in biopharmaceutical activities or other
29 biotechnology activities that are described in Codes 2833 to 2836,
30 inclusive, of the SIC Manual published by the United States Office
31 of Management and Budget, 1987 edition, and has not received
32 regulatory approval for any product from the United States Food
33 and Drug Administration.

34 (f) The credit allowed under subdivision (a) shall apply to
35 qualified property that is acquired by, or subject to lease, by a
36 qualified taxpayer, subject to the following special rules:

37 (1) A lessor of qualified property, irrespective of whether the
38 lessor is a qualified taxpayer, shall not be allowed the credit
39 provided under subdivision (a) with respect to any qualified
40 property leased to another qualified taxpayer.

(2) For purposes of paragraphs (2) and (3) of subdivision (b), “binding contract” shall include any lease agreement with respect to the qualified property.

(3) (A) For purposes of determining the qualified cost paid or incurred by a lessee in any leasing transaction that is not treated as a sale under Part 1 (commencing with Section 6001), the following rules shall apply:

(i) Except as provided by subparagraph (C) of this paragraph, subparagraphs (A) and (C) of paragraph (1) of subdivision (b) shall not apply.

(ii) Except as provided in subparagraph (B) and clause (iii), the “qualified cost” upon which the lessee shall compute the credit provided under this section shall be equal to the original cost to the lessor (within the meaning of Section 18031) of the qualified property that is the subject of the lease.

(iii) The requirement of subparagraph (B) of paragraph (1) of subdivision (b) shall be treated as satisfied only if the lessor has made a timely election under either Section 6094.1 or subdivision (d) of Section 6244 and has paid sales tax reimbursement or use tax measured by the purchase price of the qualified property (within the meaning of paragraph (5) of subdivision (g) of Section 6006). For purposes of this subdivision, the amount of original cost to the lessor which may be taken into account under clause (ii) shall not exceed the purchase price upon which sales tax reimbursement or use tax has been paid under the preceding sentence.

(iv) With respect to leases entered into between January 1, 2005 2007, and the effective date of this clause, the lessor may elect to pay use tax measured by the purchase price of the property by reporting and paying the tax with the return of the lessor for the fourth calendar quarter of 2005 2007. In computing the use tax under the preceding sentence, a credit shall be allowed under Part 1 (commencing with Section 6001) for all sales or use tax previously paid on the lease.

(B) For purposes of applying subparagraph (A) only, the following special rules shall apply:

(i) The original cost to the lessor of the qualified property shall be reduced by the amount of any original cost of that property that was taken into account by any predecessor lessee in computing the credit allowable under this section.

(ii) Clause (i) shall not apply in any case where the predecessor lessee was required to recapture the credit provided under this section pursuant to subdivision (g).

(iii) For purposes of this section only, in any case where a successor lessor has acquired qualified property from a predecessor lessor in a transaction not treated as a sale under Part 1 (commencing with Section 6001), the original cost to the successor lessor of the qualified property shall be reduced by the amount of the original cost of the qualified property that was taken into account by any lessee of the predecessor lessor in computing the credit allowable under this section.

(C) In determining the original cost of any qualified property under this paragraph, only amounts paid or incurred by the lessor on or after January 1, ~~2005~~ 2007, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i), shall be taken into account. In the case of any qualified property constructed, reconstructed, or acquired by a lessor pursuant to a binding contract in existence on or prior to January 1, ~~2005~~ 2007, the allocation rule specified in subparagraph (A) of paragraph (1) of subdivision (b) shall apply in determining the original cost to the lessor of qualified property.

(D) Notwithstanding subparagraph (A), in the case of any leasing transaction for which the lessee is allowed the credit under this section and thereafter the lessee (or any party related to the lessee within the meaning of Section 267 or 318 of the Internal Revenue Code) acquires the qualified property from the lessor (or any successor lessor), within one year from the date the qualified property is first used by the lessee under the terms of the lease, the lessee's (or related party's) acquisition of the qualified property from the lessor (or successor lessor) shall be treated as a disposition by the lessee of the qualified property that was subject to the lease under subdivision (g).

(4) For purposes of determining the qualified cost paid or incurred by a lessee in any leasing transaction that is treated as a sale under Part 1 (commencing with Section 6001), the following rules shall apply:

(A) Subparagraph (A) of paragraph (1) of subdivision (b) shall be applied by substituting the term "purchase" for the term "construction, reconstruction, or acquisition."

1 (B) Subparagraph (C) of paragraph (1) of subdivision (b) shall
2 apply.

3 (C) The requirement of subparagraph (B) of paragraph (1) of
4 subdivision (b) shall be treated as satisfied at the time that either
5 the lessor or the qualified taxpayer pays sales or use tax under Part
6 1 (commencing with Section 6001).

7 (5) (A) In the case of any leasing transaction described in
8 paragraph (3), the lessor shall provide a statement to the lessee
9 specifying the amount of the lessor's original cost of the qualified
10 property and the amount of that cost upon which a sales or use tax
11 was paid within 45 days after the close of the lessee's taxable year
12 in which the credit is allowable to the lessee under this section.

13 (B) The statement required under subparagraph (A) shall be
14 made available to the Franchise Tax Board upon request.

15 (g) No credit shall be allowed if the qualified property is
16 removed from the state, is disposed of to an unrelated party, or is
17 used for any purpose not qualifying for the credit provided in this
18 section in the same taxable year in which the qualified property is
19 first placed in service in this state. If any qualified property for
20 which a credit is allowed pursuant to this section is thereafter
21 removed from this state, disposed of to an unrelated party, or used
22 for any purpose not qualifying for the credit provided in this
23 section within one year from the date the qualified property is first
24 placed in service in this state, the amount of the credit allowed by
25 this section for that qualified property shall be recaptured by
26 adding that credit amount to the net tax of the qualified taxpayer
27 for the taxable year in which the qualified property is disposed of,
28 removed, or put to an ineligible use.

29 (h) In the case where the credit allowed by this section exceeds
30 the "net tax," the excess may be carried over to reduce the "net
31 tax" in the following year, and succeeding years as follows:

32 (1) Except as provided in paragraph (2), for the seven
33 succeeding years if necessary, until the credit is exhausted.

34 (2) In the case of a small business, for the nine succeeding
35 years, if necessary, until the credit is exhausted.

36 (i) The credit under this section shall be known as the "Career
37 Technical Education Campaign" credit or as the "CTEC" credit.

38 (j) This section shall become operative on January 1, ~~2005~~
39 ~~2007~~, and remain in effect only until January 1, ~~2012~~ 2014, and as
40 of that date is repealed.

1 ~~SEC. 6.—~~

2 *SEC. 4.* Section 23036 of the Revenue and Taxation Code is
3 amended to read:

4 23036. (a) (1) The term “tax” includes any of the following:

5 (A) The tax imposed under Chapter 2 (commencing with
6 Section 23101).

7 (B) The tax imposed under Chapter 3 (commencing with
8 Section 23501).

9 (C) The tax on unrelated business taxable income, imposed
10 under Section 23731.

11 (D) The tax on S corporations imposed under Section 23802.

12 (2) The term “tax” does not include any amount imposed
13 under paragraph (1) of subdivision (e) of Section 24667 or
14 paragraph (2) of subdivision (f) of Section 24667.

15 (b) For purposes of Article 5 (commencing with Section
16 18661) of Chapter 2, Article 3 (commencing with Section 19031)
17 of Chapter 4, Article 6 (commencing with Section 19101) of
18 Chapter 4, and Chapter 7 (commencing with Section 19501) of
19 Part 10.2, and for purposes of Sections 18601, 19001, and 19005,
20 the term “tax” shall also include all of the following:

21 (1) The tax on limited partnerships, imposed under Section
22 17935 or Section 23081, the tax on limited liability companies,
23 imposed under Section 17941 or Section 23091, and the tax on
24 registered limited liability partnerships and foreign limited
25 liability partnerships imposed under Section 17948 or Section
26 23097.

27 (2) The alternative minimum tax imposed under Chapter 2.5
28 (commencing with Section 23400).

29 (3) The tax on built-in gains of S corporations, imposed under
30 Section 23809.

31 (4) The tax on excess passive investment income of S
32 corporations, imposed under Section 23811.

33 (c) Notwithstanding any other provision of this part, credits
34 shall be allowed against the “tax” in the following order:

35 (1) Credits that do not contain carryover provisions.

36 (2) Credits that, when the credit exceeds the “tax,” allow the
37 excess to be carried over to offset the “tax” in succeeding taxable
38 years, except for those credits that are allowed to reduce the “tax”
39 below the tentative minimum tax, as defined by Section 23455.

1 The order of credits within this paragraph shall be determined by
2 the Franchise Tax Board.

3 (3) The minimum tax credit allowed by Section 23453.

4 (4) Credits that are allowed to reduce the “tax” below the
5 tentative minimum tax, as defined by Section 23455.

6 (5) Credits for taxes withheld under Section 18662.

7 (d) Notwithstanding any other provision of this part, each of
8 the following shall be applicable:

9 (1) No credit shall reduce the “tax” below the tentative
10 minimum tax (as defined by paragraph (1) of subdivision (a) of
11 Section 23455), except the following credits:

12 (A) The credit allowed by former Section 23601 (relating to
13 solar energy).

14 (B) The credit allowed by former Section 23601.4 (relating to
15 solar energy).

16 (C) The credit allowed by Section 23601.5 (relating to solar
17 energy).

18 (D) The credit allowed by Section 23609 (relating to research
19 expenditures).

20 (E) The credit allowed by Section 23609.5 (relating to clinical
21 testing expenses).

22 (F) The credit allowed by Section 23610.5 (relating to
23 low-income housing).

24 (G) The credit allowed by former Section 23612 (relating to
25 sales and use tax credit).

26 (H) The credit allowed by Section 23612.2 (relating to
27 enterprise zone sales or use tax credit).

28 (I) The credit allowed by Section 23612.6 (relating to Los
29 Angeles Revitalization Zone sales tax credit).

30 (J) The credit allowed by former Section 23622 (relating to
31 enterprise zone hiring credit).

32 (K) The credit allowed by Section 23622.7 (relating to
33 enterprise zone hiring credit).

34 (L) The credit allowed by former Section 23623 (relating to
35 program area hiring credit).

36 (M) For each taxable year beginning on or after January 1,
37 1994, the credit allowed by Section 23623.5 (relating to Los
38 Angeles Revitalization Zone hiring credit).

39 (N) The credit allowed by Section 23625 (relating to Los
40 Angeles Revitalization Zone hiring credit).

1 (O) The credit allowed by Section 23633 (relating to targeted
2 tax area sales or use tax credit).

3 (P) The credit allowed by Section 23634 (relating to targeted
4 tax area hiring credit).

5 (Q) The credit allowed by Section 23649 (relating to qualified
6 property).

7 (R) The credit allowed by Section 23651 (relating to career
8 technical education campaign).

9 (2) No credit against the tax shall reduce the minimum
10 franchise tax imposed under Chapter 2 (commencing with Section
11 23101).

12 (e) Any credit which is partially or totally denied under
13 subdivision (d) shall be allowed to be carried over to reduce the
14 “tax” in the following year, and succeeding years if necessary, if
15 the provisions relating to that credit include a provision to allow
16 a carryover of the unused portion of that credit.

17 (f) Unless otherwise provided, any remaining carryover from
18 a credit that has been repealed or made inoperative shall continue
19 to be allowed to be carried over under the provisions of that section
20 as it read immediately prior to being repealed or becoming
21 inoperative.

22 (g) Unless otherwise provided, if two or more taxpayers share
23 in costs that would be eligible for a tax credit allowed under this
24 part, each taxpayer shall be eligible to receive the tax credit in
25 proportion to its respective share of the costs paid or incurred.

26 (h) Unless otherwise provided, in the case of an S corporation,
27 any credit allowed by this part shall be computed at the S
28 corporation level, and any limitation on the expenses qualifying
29 for the credit or limitation upon the amount of the credit shall be
30 applied to the S corporation and to each shareholder.

31 (i) (1) With respect to any taxpayer that directly or indirectly
32 owns an interest in a business entity that is disregarded for tax
33 purposes pursuant to Section 23038 and any regulations
34 thereunder, the amount of any credit or credit carryforward
35 allowable for any taxable year attributable to the disregarded
36 business entity shall be limited in accordance with paragraphs (2)
37 and (3).

38 (2) The amount of any credit otherwise allowed under this part,
39 including any credit carryover from prior years, that may be
40 applied to reduce the taxpayer’s “tax,” as defined in subdivision

(a), for the taxable year shall be limited to an amount equal to the excess of the taxpayer's regular tax (as defined in Section 23455), determined by including income attributable to the disregarded business entity that generated the credit or credit carryover, over the taxpayer's regular tax (as defined in Section 23455), determined by excluding the income attributable to that disregarded business entity. No credit shall be allowed if the taxpayer's regular tax (as defined in Section 23455), determined by including the income attributable to the disregarded business entity is less than the taxpayer's regular tax (as defined in Section 23455), determined by excluding the income attributable to the disregarded business entity.

(3) If the amount of a credit allowed pursuant to the section establishing the credit exceeds the amount allowable under this subdivision in any taxable year, the excess amount may be carried over to subsequent taxable years pursuant to subdivisions (d), (e), and (f).

(j) (1) Unless otherwise specifically provided, in the case of a taxpayer that is a partner or shareholder of an eligible pass-through entity described in paragraph (2), any credit passed through to the taxpayer in the taxpayer's first taxable year beginning on or after the date the credit is no longer operative may be claimed by the taxpayer in that taxable year, notwithstanding the repeal of the statute authorizing the credit prior to the close of that taxable year.

(2) For purposes of this subdivision, "eligible pass-through entity" means any partnership or S corporation that files its return on a fiscal year basis pursuant to Section 18566, and that is entitled to a credit pursuant to this part for the taxable year that begins during the last year a credit is operative.

(3) This subdivision shall apply to credits that become inoperative on or after the operative date of the act adding this subdivision.

~~SEC. 7. Section 23649 of the Revenue and Taxation Code is amended to read:~~

~~23649. (a) (1) A qualified taxpayer shall be allowed a credit against the "tax," as defined in Section 23036, equal to the applicable percentage of the qualified cost of qualified property that is placed in service in this state. For purposes of this subdivision the applicable percentage is:~~

~~(A) Six percent for property placed in service before January 1, 2005.~~

~~(B) Five percent for property placed in service on or after January 1, 2005, and before January 1, 2006.~~

~~(C) Four percent for property placed in service on or after January 1, 2006, and before January 1, 2007.~~

~~(D) Three percent for property placed in service on or after January 1, 2007, and before January 1, 2008.~~

~~(E) Two percent for property placed in service on or after January 1, 2008, and before January 1, 2009.~~

~~(F) One percent for property placed in service on or after January 1, 2009, and before January 1, 2010.~~

~~(2) In the case of any qualified costs paid or incurred on or after January 1, 1994, and prior to the first taxable year of the qualified taxpayer beginning on or after January 1, 1995, the credit provided under paragraph (1) shall be claimed by the qualified taxpayer on the qualified taxpayer's return for the first taxable year beginning on or after January 1, 1995. No credit shall be claimed under this section on a return filed for any taxable year commencing prior to the qualified taxpayer's first taxable year beginning on or after January 1, 1995.~~

~~(b) (1) For purposes of this section, "qualified cost" means any cost that satisfies each of the following conditions:~~

~~(A) Except as otherwise provided in this subparagraph, is a cost paid or incurred by the qualified taxpayer for the construction, reconstruction, or acquisition of qualified property on or after January 1, 1994, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i). In the case of any qualified property constructed, reconstructed, or acquired by the qualified taxpayer (or any person related to the qualified taxpayer within the meaning of Section 267 or 707 of the Internal Revenue Code) pursuant to a binding contract in existence on or prior to January 1, 1994, costs paid pursuant to that contract shall be subject to allocation as follows: contract costs shall be allocated to qualified property based on a ratio of costs actually paid prior to January 1, 1994, and total contract costs actually paid. "Cost paid" shall include, without limitation, contractual deposits and option payments. To the extent of cost allocated, whether or not currently deductible or depreciable for tax purposes, to a period prior to~~

1 ~~January 1, 1994, the cost shall be deemed allocated to property~~
2 ~~acquired before January 1, 1994, and is thus not a “qualified cost.”~~

3 ~~(B) Except as provided in paragraph (3) of subdivision (d) and~~
4 ~~subparagraph (B) of paragraph (4) of subdivision (d), is an amount~~
5 ~~upon which the qualified taxpayer has paid, directly or indirectly~~
6 ~~as a separately stated contract amount or as determined from the~~
7 ~~records of the qualified taxpayer, sales or use tax under Part 1~~
8 ~~(commencing with Section 6001).~~

9 ~~(C) Is an amount properly chargeable to the capital account of~~
10 ~~the qualified taxpayer.~~

11 ~~(2) (A) For purposes of this subdivision, any contract entered~~
12 ~~into on or after January 1, 1994, that is a successor or replacement~~
13 ~~contract to a contract that was binding prior to January 1, 1994,~~
14 ~~shall be treated as a binding contract in existence prior to January~~
15 ~~1, 1994.~~

16 ~~(B) If a successor or replacement contract is entered into on or~~
17 ~~after January 1, 1994, and the subject of the successor or~~
18 ~~replacement contract relates both to amounts for the construction,~~
19 ~~reconstruction, or acquisition of qualified property described in~~
20 ~~the original binding contract and to costs for the construction,~~
21 ~~reconstruction, or acquisition of qualified property not described~~
22 ~~in the original binding contract, then the portion of those amounts~~
23 ~~described in the successor or replacement contract that were not~~
24 ~~described in the original binding contract shall not be treated as~~
25 ~~costs paid or incurred pursuant to a binding contract in existence~~
26 ~~on or prior to January 1, 1994, under subparagraph (A) of~~
27 ~~paragraph (1).~~

28 ~~(3) (A) For purposes of this section, an option contract in~~
29 ~~existence prior to January 1, 1994, under which a qualified~~
30 ~~taxpayer (or any other person related to the qualified taxpayer~~
31 ~~within the meaning of Section 267 or 707 of the Internal Revenue~~
32 ~~Code) had an option to acquire qualified property, shall be treated~~
33 ~~as a binding contract under the rules in paragraph (2). For purposes~~
34 ~~of this subparagraph, an option contract shall not include an option~~
35 ~~under which the optionholder will forfeit an amount less than 10~~
36 ~~percent of the fixed option price in the event the option is not~~
37 ~~exercised.~~

38 ~~(B) For purposes of this section, a contract shall be treated as~~
39 ~~binding even if the contract is subject to a condition.~~

~~(4) For purposes of this subdivision, in the case of any qualified taxpayer engaged in those lines of business described in Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, “the first taxable year beginning on or after January 1, 1998,” shall be substituted for “January 1, 1994,” in each place in which it appears.~~

~~(c) (1) For purposes of this section, “qualified taxpayer” means any taxpayer engaged in those lines of business described in Codes 2011 to 3999, inclusive, or Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition.~~

~~(2) In the case of any passthrough entity, the determination of whether a taxpayer is a qualified taxpayer shall be made at the entity level and any credit under this section or Section 17053.49 shall be allowed to the passthrough entity and passed through to the partners or shareholders in accordance with applicable provisions of Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001). For purposes of this paragraph, the term “passthrough entity” means any partnership or S corporation.~~

~~(3) The Franchise Tax Board may prescribe regulations to carry out the purposes of this section, including any regulations necessary to prevent the avoidance of the effect of this section through splitups, shell corporations, partnerships, tiered ownership structures, sale-leaseback transactions, or otherwise.~~

~~(d) For purposes of this section, “qualified property” means property that is described as either of the following:~~

~~(1) Tangible personal property that is defined in Section 1245(a) of the Internal Revenue Code for use by a qualified taxpayer in those lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, that is primarily used for any of the following:~~

~~(A) For the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the process and ending at the point at which the~~

1 manufacturing, processing, refining, fabricating, or recycling has
2 altered tangible personal property to its completed form, including
3 packaging, if required.

4 (B) In research and development.

5 (C) To maintain, repair, measure, or test any property described
6 in this paragraph.

7 (D) For pollution control that meets or exceeds standards
8 established by the state or by any local or regional governmental
9 agency within the state.

10 (E) For recycling.

11 (2) Computers and computer peripheral equipment, as defined
12 in Section 168(i)(2)(B) of the Internal Revenue Code, that is
13 tangible personal property as defined in Section 1245(a) of the
14 Internal Revenue Code for use by a qualified taxpayer in those
15 lines of business described in SIC Codes 7371 to 7373, inclusive,
16 of the SIC Manual, 1987 edition, that is primarily used to develop
17 or manufacture prepackaged software or custom software
18 prepared to the special order of the purchaser who uses the
19 program to produce and sell or license copies of the program as
20 prepackaged software.

21 (3) The value of any capitalized labor costs that are directly
22 allocable to the construction or modification of property described
23 in paragraph (1) or (2).

24 (4) In the case of any qualified taxpayer engaged in
25 manufacturing activities described in SIC Code 357 or 367, those
26 activities related to biotechnology described in SIC Code 8731,
27 those activities related to biopharmaceutical establishments only
28 that are described in SIC Codes 2833 to 2836, inclusive, those
29 activities related to space vehicles and parts described in SIC
30 Codes 3761 to 3769, inclusive, those activities related to space
31 satellites and communications satellites and equipment described
32 in SIC Codes 3663 and 3812 (but only with respect to “qualified
33 property” that is placed in service on or after January 1, 1996), or
34 those activities related to semiconductor equipment
35 manufacturing described in SIC Code 3559 (but only with respect
36 to “qualified property” that is placed in service on or after January
37 1, 1997), “qualified property” also includes the following:

38 (A) Special purpose buildings and foundations that are
39 constructed or modified for use by the qualified taxpayer primarily
40 in a manufacturing, processing, refining, or fabricating process, or

1 as a research or storage facility primarily used in connection with
2 a manufacturing process.

3 (B) The value of any capitalized labor costs that are directly
4 allocable to the construction or modification of special purpose
5 buildings and foundations that are used primarily in the
6 manufacturing, processing, refining, or fabricating process, or as
7 a research or storage facility primarily used in connection with a
8 manufacturing process.

9 (C) (i) For purposes of this paragraph, “special purpose
10 building and foundation” means only a building and the
11 foundation immediately underlying the building that is
12 specifically designed and constructed or reconstructed for the
13 installation, operation, and use of specific machinery and
14 equipment with a special purpose, which machinery and
15 equipment, after installation, will become affixed to or a fixture of
16 the real property, and the construction or reconstruction of which
17 is specifically designed and used exclusively for the specified
18 purposes as set forth in subparagraph (A) (“qualified purpose”).

19 (ii) A building is specifically designed and constructed or
20 modified for a qualified purpose if it is not economical to design
21 and construct the building for the intended purpose and then use
22 the structure for a different purpose.

23 (iii) For purposes of clause (i) and clause (vi), a building is used
24 exclusively for a qualified purpose only if its use does not include
25 a use for which it was not specifically designed and constructed or
26 modified. Incidental use of a building for nonqualified purposes
27 does not preclude the building from being a special purpose
28 building. “Incidental use” means a use which is both related and
29 subordinate to the qualified purpose. It will be conclusively
30 presumed that a use is not subordinate if more than one third of the
31 total usable volume of the building is devoted to a use which is not
32 a qualified purpose.

33 (iv) In the event an entire building does not qualify as a special
34 purpose building, a taxpayer may establish that a portion of a
35 building, and the foundation immediately underlying the portion,
36 qualifies for treatment as a special purpose building and
37 foundation if the portion satisfies all of the definitional provisions
38 in this subparagraph.

39 (v) To the extent that a building is not a special purpose
40 building as defined above, but a portion of the building qualifies

1 for treatment as a special purpose building, then all equipment
2 which exclusively supports the qualified purpose occurring within
3 that portion and which would qualify as Internal Revenue Code
4 Section 1245 property if it were not a fixture or affixed to the
5 building shall be treated as a cost of the portion of the building
6 which qualifies for treatment as a special purpose building.

7 (vi) Buildings and foundations which do not meet the
8 definition of a special purpose building and foundation set forth
9 above include, but are not limited to: buildings designed and
10 constructed or reconstructed principally to function as a general
11 purpose manufacturing, industrial, or commercial building;
12 research facilities that are used primarily prior to or after, or prior
13 to and after, the manufacturing process; or storage facilities that
14 are used primarily prior to or after, or prior to and after, completion
15 of the manufacturing process. A research facility shall not be
16 considered to be used primarily prior to or after, or prior to and
17 after, the manufacturing process if its purpose and use relate
18 exclusively to the development and regulatory approval of the
19 manufacturing process for specific biopharmaceutical products. A
20 research facility which is used primarily in connection with the
21 discovery of an organism from which a biopharmaceutical product
22 or process is developed does not meet the requirements of the
23 preceding sentence.

24 (5) Subject to the provisions in subparagraph (B) of paragraph
25 (1) of subdivision (b), qualified property also includes computer
26 software that is primarily used for those purposes set forth in
27 paragraph (1) or (2) of this subdivision.

28 (6) Qualified property does not include any of the following:

29 (A) Furniture.

30 (B) Facilities used for warehousing purposes after completion
31 of the manufacturing process.

32 (C) Inventory.

33 (D) Equipment used in the extraction process.

34 (E) Equipment used to store finished products that have
35 completed the manufacturing process.

36 (F) Any tangible personal property that is used in
37 administration, general management, or marketing.

38 (G) Any vehicle for which a credit is claimed pursuant to
39 Section 17052.11 or 23603.

40 (e) For purposes of this section:

~~(1) “Biopharmaceutical activities” means those activities that use organisms or materials derived from organisms, and their cellular, subcellular, or molecular components, in order to provide pharmaceutical products for human or animal therapeutics and diagnostics. Biopharmaceutical activities make use of living organisms to make commercial products, as opposed to pharmaceutical activities which make use of chemical compounds to produce commercial products.~~

~~(2) “Fabricating” means to make, build, create, produce, or assemble components or property to work in a new or different manner.~~

~~(3) “Manufacturing” means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.~~

~~(4) “Other biotechnology activities” means activities consisting of the application of recombinant DNA technology to produce commercial products, as well as activities regarding pharmaceutical delivery systems designed to provide a measure of control over the rate, duration, and site of pharmaceutical delivery.~~

~~(5) “Primarily” means tangible personal property used 50 percent or more of the time in an activity described in subdivision (d).~~

~~(6) “Process” means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer’s manufacturing, processing, refining, fabricating, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified taxpayer’s manufacturing, processing, refining, fabricating, or recycling activity is~~

1 conducted, shall not be considered to have been introduced into the
2 manufacturing, processing, refining, fabricating, or recycling
3 process.

4 (7) “Processing” means the physical application of the
5 materials and labor necessary to modify or change the
6 characteristics of property.

7 (8) “Refining” means the process of converting a natural
8 resource to an intermediate or finished product.

9 (9) “Research and development” means those activities that
10 are described in Section 174 of the Internal Revenue Code or in any
11 regulations thereunder.

12 (10) “Small business” means a qualified taxpayer that meets
13 any of the following requirements during the taxable year for
14 which the credit is allowed:

15 (A) Has gross receipts of less than fifty million dollars
16 (\$50,000,000).

17 (B) Has net assets of less than fifty million dollars
18 (\$50,000,000).

19 (C) Has a total credit of less than one million dollars
20 (\$1,000,000).

21 (D) For taxable years beginning on or after January 1, 1997, is
22 engaged in biopharmaceutical activities or other biotechnology
23 activities that are described in Codes 2833 to 2836, inclusive, of
24 the Standard Industrial Classification (SIC) Manual published by
25 the United States Office of Management and Budget, 1987 edition,
26 and has not received regulatory approval for any product from the
27 United States Food and Drug Administration.

28 (f) The credit allowed under subdivision (a) shall apply to
29 qualified property that is acquired by or subject to lease by a
30 qualified taxpayer, subject to the following special rules:

31 (1) A lessor of qualified property, irrespective of whether the
32 lessor is a qualified taxpayer, shall not be allowed the credit
33 provided under subdivision (a) with respect to any qualified
34 property leased to another qualified taxpayer.

35 (2) For purposes of paragraphs (2) and (3) of subdivision (b),
36 “binding contract” shall include any lease agreement with respect
37 to the qualified property.

38 (3) (A) For purposes of determining the qualified cost paid or
39 incurred by a lessee in any leasing transaction that is not treated as

1 a sale under Part 1 (commencing with Section 6001), the following
2 rules shall apply:

3 (i) Except as provided by subparagraph (C) of this paragraph,
4 subparagraphs (A) and (C) of paragraph (1) of subdivision (b)
5 shall not apply.

6 (ii) Except as provided in subparagraph (B) and clause (iii), the
7 “qualified cost” upon which the lessee shall compute the credit
8 provided under this section shall be equal to the original cost to the
9 lessor (within the meaning of Section 24912) of the qualified
10 property that is the subject of the lease.

11 (iii) Except as provided in clause (iv), the requirement of
12 subparagraph (B) of paragraph (1) of subdivision (b) shall be
13 treated as satisfied only if the lessor has made a timely election
14 under either Section 6094.1 or subdivision (d) of Section 6244 and
15 has paid sales tax reimbursement or use tax measured by the
16 purchase price of the qualified property (within the meaning of
17 paragraph (5) of subdivision (g) of Section 6006). For purposes of
18 this subdivision and clause (iv), the amount of original cost to the
19 lessor which may be taken into account under clause (ii) shall not
20 exceed the purchase price upon which sales tax reimbursement or
21 use tax has been paid under the preceding sentence or under clause
22 (iv).

23 (iv) With respect to leases entered into between January 1,
24 1994, and the effective date of this clause, the lessor may elect to
25 pay use tax measured by the purchase price of the property by
26 reporting and paying the tax with the return of the lessor for the
27 fourth calendar quarter of 1994. In computing the use tax under the
28 preceding sentence, a credit shall be allowed under Part 1
29 (commencing with Section 6001) for all sales or use tax previously
30 paid on the lease.

31 (B) For purposes of applying subparagraph (A) only, the
32 following special rules shall apply:

33 (i) The original cost to the lessor of the qualified property shall
34 be reduced by the amount of any original cost of that property that
35 was taken into account by any predecessor lessee in computing the
36 credit allowable under this section.

37 (ii) Clause (i) shall not apply in any case where the predecessor
38 lessee was required to recapture the credit provided under this
39 section pursuant to subdivision (g).

~~(iii) For purposes of this section only, in any case where a successor lessor has acquired qualified property from a predecessor lessor in a transaction not treated as a sale under Part 1 (commencing with Section 6001), the original cost to the successor lessor of the qualified property shall be reduced by the amount of the original cost of the qualified property that was taken into account by any lessee of the predecessor lessor in computing the credit allowable under this section.~~

~~(C) In determining the original cost of any qualified property under this paragraph, only amounts paid or incurred by the lessor on or after January 1, 1994, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i), shall be taken into account. In the case of any qualified property constructed, reconstructed, or acquired by a lessor pursuant to a binding contract in existence on or prior to January 1, 1994, the allocation rule specified in subparagraph (A) of paragraph (1) of subdivision (b) shall apply in determining the original cost to the lessor of qualified property.~~

~~(D) Notwithstanding subparagraph (A), in the case of any leasing transaction for which the lessee is allowed the credit under this section and thereafter the lessee (or any party related to the lessee within the meaning of Section 267 or 318 of the Internal Revenue Code) acquires the qualified property from the lessor (or any successor lessor) within one year from the date the qualified property is first used by the lessee under the terms of the lease, the lessee's (or related party's) acquisition of the qualified property from the lessor (or successor lessor) shall be treated as a disposition by the lessee of the qualified property that was subject to the lease under subdivision (g).~~

~~(4) For purposes of determining the qualified cost paid or incurred by a lessee in any leasing transaction that is treated as a sale under Part 1 (commencing with Section 6001), the following rules shall apply:~~

~~(A) Subparagraph (A) of paragraph (1) of subdivision (b) shall be applied by substituting the term "purchase" for the term "construction, reconstruction, or acquisition."~~

~~(B) Subparagraph (C) of paragraph (1) of subdivision (b) shall apply.~~

~~(C) The requirement of subparagraph (B) of paragraph (1) of subdivision (b) shall be treated as satisfied at the time that either~~

~~the lessor or the qualified taxpayer pays sales or use tax under Part 1 (commencing with Section 6001).~~

~~(5) (A) In the case of any leasing transaction described in paragraph (3), the lessor shall provide a statement to the lessee specifying the amount of the lessor's original cost of the qualified property and the amount of that cost upon which a sales or use tax was paid within 45 days after the close of the lessee's taxable year in which the credit is allowable to the lessee under this section.~~

~~(B) The statement required under subparagraph (A) shall be made available to the Franchise Tax Board upon request.~~

~~(6) For purposes of this subdivision, in the case of any qualified taxpayer engaged in those lines of business described in Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition, "the first taxable year beginning on or after January 1, 1998," shall be substituted for "January 1, 1994," in each place in which it appears. In addition, "the effective date of this paragraph" shall be substituted for "the effective date of this clause" and "fourth calendar quarter of 1998" shall be substituted for "fourth calendar quarter of 1994."~~

~~(g) No credit shall be allowed if the qualified property is removed from the state, is disposed of to an unrelated party, or is used for any purpose not qualifying for the credit provided in this section in the same taxable year in which the qualified property is first placed in service in this state. If any qualified property for which a credit is allowed pursuant to this section is thereafter removed from this state, disposed of to an unrelated party, or used for any purpose not qualifying for the credit provided in this section within one year from the date the qualified property is first placed in service in this state, the amount of the credit allowed by this section for that qualified property shall be recaptured by adding that credit amount to the net tax of the qualified taxpayer for the taxable year in which the qualified property is disposed of, removed, or put to an ineligible use. The sale of stock for which an election was made or deemed to have been made pursuant to Section 338(g) or 338(h)(10) of the Internal Revenue Code may not be treated as a disposition of qualified property to an unrelated party for purposes of this subdivision.~~

~~(h) In the case where the credit allowed by this section exceeds the “tax,” the excess may be carried over to reduce the “tax” in the following year, and succeeding years as follows:~~

~~(1) Except as provided in paragraph (2), for the seven succeeding years if necessary, until the credit is exhausted.~~

~~(2) In the case of a small business, for the nine succeeding years, if necessary, until the credit is exhausted.~~

~~(i) (1) This section shall remain in effect until the date specified in paragraph (2) on which date this section shall cease to be operative, and as of that date is repealed.~~

~~(2) This section shall cease to be operative on January 1, 2011.~~

~~(j) The amendments made by Chapter 954 of the Statutes of 1996 shall be operative for taxable years beginning on or after January 1, 1997, except as provided in paragraph (3) of subdivision (d).~~

~~(k) The amendments made by Chapter 323 of the Statutes of 1998 shall be operative for taxable years beginning on or after January 1, 1998.~~

~~SEC. 8.—~~

SEC. 5. Section 23651 is added to the Revenue and Taxation Code, to read:

23651. (a) A qualified taxpayer shall be allowed a credit against the “tax,” as defined in Section 23036, in an amount equal to 6 percent of the qualified cost of qualified property that is placed in service in this state. For purposes of this subdivision, the applicable percentage is:

~~(1) Two One percent for property placed in service on or after January 1, 2005, and before January 1, 2006.~~

~~(2) Three percent for property placed in service e on or after January 1, 2006, and before January 1, 2007.~~

~~(3) Four percent for property placed in service on or after January 1, 2007, and before January 1, 2008.~~

~~(4) Five perecent for property placed in service on or after January 1, 2008, and before January 1, 2009.~~

~~(5) Six percent for property placed in service on or after January 1, 2009, and before January 1, 2010.~~

~~(6) January 1, 2007, and before January 1, 2009.~~

(2) Four percent for property placed in service on or after January 1, 2009, and before January 1, 2010.

1 (3) Seven percent for property placed in service on or after
2 January 1, 2010.

3 (b) (1) For purposes of this section, “qualified cost” means
4 any cost that satisfies each of the following conditions:

5 (A) Except as otherwise provided in this subparagraph, is a cost
6 paid or incurred by the qualified taxpayer for the construction,
7 reconstruction, or acquisition of qualified property on or after
8 January 1, ~~2005~~ 2007, and prior to the date this section ceases to
9 be operative under paragraph (2) of subdivision (i). In the case of
10 any qualified property constructed, reconstructed, or acquired by
11 the qualified taxpayer (or any person related to the qualified
12 taxpayer within the meaning of Section 267 or 707 of the Internal
13 Revenue Code) pursuant to a binding contract in existence on or
14 prior to January 1, ~~2005~~ 2007, costs paid pursuant to that contract
15 shall be subject to allocation as follows: contract costs shall be
16 allocated to qualified property based on a ratio of costs actually
17 paid prior to January 1, ~~2005~~ 2007, and total contract costs actually
18 paid. “Cost paid” shall include, without limitation, contractual
19 deposits and option payments. To the extent of cost allocated,
20 whether or not currently deductible or depreciable for tax
21 purposes, to a period prior to January 1, ~~2005~~ 2007, the cost shall
22 be deemed allocated to property acquired before January 1, ~~2005~~
23 2007, and is thus not a “qualified cost.”

24 (B) Except as provided in paragraph (3) of subdivision (d) and
25 subparagraph (B) of paragraph (4) of subdivision (d), is an amount
26 upon which the qualified taxpayer has paid, directly or indirectly,
27 as a separately stated contract amount or as determined from the
28 records of the qualified taxpayer, sales or use tax under Part 1
29 (commencing with Section 6001).

30 (C) Is an amount properly chargeable to the capital account of
31 the qualified taxpayer.

32 (2) (A) For purposes of this subdivision, any contract entered
33 into on or after January 1, ~~2005~~ 2007, that is a successor or
34 replacement contract to a contract that was binding prior to
35 January 1, ~~2005~~ 2007, shall be treated as a binding contract in
36 existence prior to January 1, ~~2005~~ 2007.

37 (B) If a successor or replacement contract is entered into on or
38 after January 1, ~~2005~~ 2007, and the subject of the successor or
39 replacement contract relates both to amounts for the construction,
40 reconstruction, or acquisition of qualified property described in

the original binding contract and to costs for the construction, reconstruction, or acquisition of qualified property not described in the original binding contract, then the portion of those amounts described in the successor or replacement contract that were not described in the original binding contract shall not be treated as costs paid or incurred pursuant to a binding contract in existence on or prior to January 1, ~~2005~~ 2007, under subparagraph (A) of paragraph (1).

(3) (A) For purposes of this section, an option contract in existence prior to January 1, ~~2005~~ 2007, under which a qualified taxpayer (or any other person related to the qualified taxpayer within the meaning of Section 267 or 707 of the Internal Revenue Code) had an option to acquire qualified property, shall be treated as a binding contract under the rules in paragraph (2). For purposes of this subparagraph, an option contract shall not include an option under which the optionholder will forfeit an amount less than 10 percent of the fixed option price in the event the option is not exercised.

(B) For purposes of this section, a contract shall be treated as binding even if the contract is subject to a condition.

(c) (1) For purposes of this section, “qualified taxpayer” means any taxpayer that is both of the following:

(A) Engaged in those lines of business described in Codes 2011 to 3999, inclusive, or Codes 7371 to 7373, inclusive, of the Standard Industrial Classification (SIC) Manual published by the United States Office of Management and Budget, 1987 edition.

(B) Certified, in the form and manner prescribed by the State Department of Education, as a qualified participant in the Career Technical Education Campaign pursuant to Section 52337 of the Education Code for the taxable year for which a credit is claimed under this section.

(2) In the case of any passthrough entity, the determination of whether a taxpayer is a qualified taxpayer under this section or Section 17053.51 shall be allowed to the passthrough entity and passed through to the partners or shareholders in accordance with applicable provisions of Part 10 (commencing with Section 17001) or this part. For purposes of this paragraph, the term “passthrough entity” means any partnership or S corporation.

(3) The Franchise Tax Board may prescribe regulations to carry out the purposes of this section, including any regulations

1 necessary to prevent the avoidance of the effect of this section
2 through splitups, shell corporations, partnerships, tiered
3 ownership structures, sale-leaseback transactions, or otherwise.

4 (d) For purposes of this section, “qualified property” means
5 property that is described as any of the following:

6 (1) Tangible personal property that is defined in Section
7 1245(a) of the Internal Revenue Code for use by a qualified
8 taxpayer in those lines of business described in Codes 2011 to
9 3999, inclusive, of the SIC Manual published by the United States
10 Office of Management and Budget, 1987 edition, that is primarily
11 used for any of the following:

12 (A) For the manufacturing, processing, refining, fabricating, or
13 recycling of property, beginning at the point at which any raw
14 materials are received by the qualified taxpayer and introduced
15 into the process and ending at the point at which the
16 manufacturing, processing, refining, fabricating, or recycling has
17 altered tangible personal property to its completed form, including
18 packaging, if required.

19 (B) In research and development.

20 (C) To maintain, repair, measure, or test any property described
21 in this paragraph.

22 (D) For pollution control that meets or exceeds standards
23 established by the state or by any local or regional governmental
24 agency within the state.

25 (E) For recycling.

26 (2) Computers and computer peripheral equipment, as defined
27 in Section 168(i)(2)(B) of the Internal Revenue Code, that is
28 tangible personal property as defined in Section 1245(a) of the
29 Internal Revenue Code for use by a qualified taxpayer in those
30 lines of business described in SIC Codes 7371 to 7373, inclusive,
31 of the SIC Manual, 1987 edition, that is primarily used to develop
32 or manufacture prepackaged software or custom software
33 prepared to the special order of the purchaser who uses the
34 program to produce and sell or license copies of the program as
35 prepackaged software.

36 (3) The value of any capitalized labor costs that are directly
37 allocable to the construction or modification of property described
38 in paragraph (1) or (2).

39 (4) In the case of any qualified taxpayer engaged in
40 manufacturing activities described in SIC Code 357 or 367, those

1 activities related to biotechnology described in SIC Code 8731,
2 those activities related to biopharmaceutical establishments only
3 that are described in SIC Codes 2833 to 2836, inclusive, those
4 activities related to space vehicles and parts described in SIC
5 Codes 3761 to 3769, inclusive, those activities related to space
6 satellites and communications satellites and equipment described
7 in SIC Codes 3663 and 3812, or those activities related to
8 semiconductor equipment manufacturing described in SIC Code
9 3559, “qualified property” also includes the following:

10 (A) Special purpose buildings and foundations that are
11 constructed or modified for use by the qualified taxpayer primarily
12 in a manufacturing, processing, refining, or fabricating process, or
13 as a research or storage facility primarily used in connection with
14 a manufacturing process.

15 (B) The value of any capitalized labor costs that are directly
16 allocable to the construction or modification of special purpose
17 buildings and foundations that are used primarily in the
18 manufacturing, processing, refining, or fabricating process, or as
19 a research or storage facility primarily used in connection with a
20 manufacturing process.

21 (C) (i) For purposes of this paragraph, “special purpose
22 building and foundation” means only a building and the
23 foundation immediately underlying the building that is
24 specifically designed and constructed or reconstructed for the
25 installation, operation, and use of specific machinery and
26 equipment with a special purpose, which machinery and
27 equipment, after installation, will become affixed to or a fixture of
28 the real property, and the construction or reconstruction of which
29 is specifically designed and used exclusively for the specified
30 purposes as set forth in subparagraph (A).

31 (ii) A building is specifically designed and constructed or
32 modified for a qualified purpose if it is not economical to design
33 and construct the building for the intended purpose and then use
34 the structure for a different purpose.

35 (iii) For purposes of clause (i) and clause (vi), a building is used
36 exclusively for a qualified purpose only if its use does not include
37 a use for which it was not specifically designed and constructed or
38 modified. Incidental use of a building for nonqualified purposes
39 does not preclude the building from being a special purpose
40 building. “Incidental use” means a use which is both related and



1 subordinate to the qualified purpose. It will be conclusively
2 presumed that a use is not subordinate if more than one-third of the
3 total usable volume of the building is devoted to a use which is not
4 a qualified purpose.

5 (iv) In the event an entire building does not qualify as a special
6 purpose building, a taxpayer may establish that a portion of a
7 building, and the foundation immediately underlying the portion,
8 qualifies for treatment as a special purpose building and
9 foundation if the portion satisfies all of the definitional provisions
10 in this subparagraph.

11 (v) To the extent that a building is not a special purpose
12 building as defined above, but a portion of the building qualifies
13 for treatment as a special purpose building, then all equipment
14 which exclusively supports the qualified purpose occurring within
15 that portion and which would qualify as Internal Revenue Code
16 Section 1245 property if it were not a fixture or affixed to the
17 building shall be treated as a cost of the portion of the building
18 which qualifies for treatment as a special purpose building.

19 (vi) Buildings and foundations which do not meet the
20 definition of a special purpose building and foundation set forth
21 above include, but are not limited to: buildings designed and
22 constructed or reconstructed principally to function as a general
23 purpose manufacturing, industrial, or commercial building;
24 research facilities that are used primarily prior to or after, or prior
25 to and after, the manufacturing process; or storage facilities that
26 are used primarily prior to or after, or prior to and after, completion
27 of the manufacturing process. A research facility shall not be
28 considered to be used primarily prior to or after, or prior to and
29 after, the manufacturing process if its purpose and use relate
30 exclusively to the development and regulatory approval of the
31 manufacturing process for specific biopharmaceutical products. A
32 research facility which is used primarily in connection with the
33 discovery of an organism from which a biopharmaceutical product
34 or process is developed does not meet the requirements of the
35 preceding sentence.

36 (5) Subject to the provisions in subparagraph (B) of paragraph
37 (1) of subdivision (b), qualified property also includes computer
38 software that is primarily used for those purposes set forth in
39 paragraph (1) or (2) of this subdivision.

40 (6) Qualified property does not include any of the following:

1 (A) Furniture.

2 (B) Facilities used for warehousing purposes after completion
3 of the manufacturing process.

4 (C) Inventory.

5 (D) Equipment used in the extraction process.

6 (E) Equipment used to store finished products that have
7 completed the manufacturing process.

8 (F) Any tangible personal property that is used in
9 administration, general management, or marketing.

10 (e) For purposes of this section:

11 (1) “Biopharmaceutical activities” means those activities that
12 use organisms or materials derived from organisms, and their
13 cellular, subcellular, or molecular components, in order to provide
14 pharmaceutical products for human or animal therapeutics and
15 diagnostics. Biopharmaceutical activities make use of living
16 organisms to make commercial products, as opposed to
17 pharmaceutical activities which make use of chemical compounds
18 to produce commercial products.

19 (2) “Fabricating” means to make, build, create, produce, or
20 assemble components or property to work in a new or different
21 manner.

22 (3) “Manufacturing” means the activity of converting or
23 conditioning property by changing the form, composition, quality,
24 or character of the property for ultimate sale at retail or use in the
25 manufacturing of a product to be ultimately sold at retail.
26 Manufacturing includes any improvements to tangible personal
27 property that result in a greater service life or greater functionality
28 than that of the original property.

29 (4) “Other biotechnology activities” means activities
30 consisting of the application of recombinant DNA technology to
31 produce commercial products, as well as activities regarding
32 pharmaceutical delivery systems designed to provide a measure of
33 control over the rate, duration, and site of pharmaceutical delivery.

34 (5) “Primarily” means tangible personal property used 50
35 percent or more of the time in an activity described in subdivision
36 (d).

37 (6) “Process” means the period beginning at the point at which
38 any raw materials are received by the qualified taxpayer and
39 introduced into the manufacturing, processing, refining,
40 fabricating, or recycling activity of the qualified person and

1 ending at the point at which the manufacturing, processing,
2 refining, fabricating, or recycling activity of the qualified taxpayer
3 has altered tangible personal property to its completed form,
4 including packaging, if required. Raw materials shall be
5 considered to have been introduced into the process when the raw
6 materials are stored on the same premises where the qualified
7 taxpayer's manufacturing, processing, refining, fabricating, or
8 recycling activity is conducted. Raw materials that are stored on
9 premises other than where the qualified taxpayer's manufacturing,
10 processing, refining, fabricating, or recycling activity is
11 conducted, shall not be considered to have been introduced into the
12 manufacturing, processing, refining, fabricating, or recycling
13 process.

14 (7) "Processing" means the physical application of the
15 materials and labor necessary to modify or change the
16 characteristics of property.

17 (8) "Refining" means the process of converting a natural
18 resource to an intermediate or finished product.

19 (9) "Research and development" means those activities that
20 are described in Section 174 of the Internal Revenue Code or in any
21 regulations thereunder.

22 (10) "Small business" means a qualified taxpayer that meets
23 any of the following requirements during the taxable year for
24 which the credit is allowed:

25 (A) Has gross receipts of less than fifty million dollars
26 (\$50,000,000).

27 (B) Has net assets of less than fifty million dollars
28 (\$50,000,000).

29 (C) Has a total credit of less than one million dollars
30 (\$1,000,000).

31 (D) Is engaged in biopharmaceutical activities or other
32 biotechnology activities that are described in Codes 2833 to 2836,
33 inclusive, of the Standard Industrial Classification (SIC) Manual
34 published by the United States Office of Management and Budget,
35 1987 edition, and has not received regulatory approval for any
36 product from the United States Food and Drug Administration.

37 (f) The credit allowed under subdivision (a) shall apply to
38 qualified property that is acquired by or subject to lease by a
39 qualified taxpayer, subject to the following special rules:

1 (1) A lessor of qualified property, irrespective of whether the
2 lessor is a qualified taxpayer, shall not be allowed the credit
3 provided under subdivision (a) with respect to any qualified
4 property leased to another qualified taxpayer.

5 (2) For purposes of paragraphs (2) and (3) of subdivision (b),
6 “binding contract” shall include any lease agreement with respect
7 to the qualified property.

8 (3) (A) For purposes of determining the qualified cost paid or
9 incurred by a lessee in any leasing transaction that is not treated as
10 a sale under Part 1 (commencing with Section 6001), the following
11 rules shall apply:

12 (i) Except as provided by subparagraph (C) of this paragraph,
13 subparagraphs (A) and (C) of paragraph (1) of subdivision (b)
14 shall not apply.

15 (ii) Except as provided in subparagraph (B) and clause (iii), the
16 “qualified cost” upon which the lessee shall compute the credit
17 provided under this section shall be equal to the original cost to the
18 lessor (within the meaning of Section 18031) of the qualified
19 property that is the subject of the lease.

20 (iii) Except as provided in clause (iv), the requirement of
21 subparagraph (B) of paragraph (1) of subdivision (b) shall be
22 treated as satisfied only if the lessor has made a timely election
23 under either Section 6094.1 or subdivision (d) of Section 6244 and
24 has paid sales tax reimbursement or use tax measured by the
25 purchase price of the qualified property (within the meaning of
26 paragraph (5) of subdivision (g) of Section 6006). For purposes of
27 this subdivision and clause (iv), the amount of original cost to the
28 lessor which may be taken into account under clause (ii) shall not
29 exceed the purchase price upon which sales tax reimbursement or
30 use tax has been paid under the preceding sentence or under clause
31 (iv).

32 (iv) With respect to leases entered into between January 1, 2005
33 2007, and the effective date of this clause, the lessor may elect to
34 pay use tax measured by the purchase price of the property by
35 reporting and paying the tax with the return of the lessor for the
36 fourth calendar quarter of ~~2005~~ 2007. In computing the use tax
37 under the preceding sentence, a credit shall be allowed under Part
38 1 (commencing with Section 6001) for all sales or use tax
39 previously paid on the lease.

(B) For purposes of applying subparagraph (A) only, the following special rules shall apply:

(i) The original cost to the lessor of the qualified property shall be reduced by the amount of any original cost of that property that was taken into account by any predecessor lessee in computing the credit allowable under this section.

(ii) Clause (i) shall not apply in any case where the predecessor lessee was required to recapture the credit provided under this section pursuant to subdivision (g).

(iii) For purposes of this section only, in any case where a successor lessor has acquired qualified property from a predecessor lessor in a transaction not treated as a sale under Part 1 (commencing with Section 6001), the original cost to the successor lessor of the qualified property shall be reduced by the amount of the original cost of the qualified property that was taken into account by any lessee of the predecessor lessor in computing the credit allowable under this section.

(C) In determining the original cost of any qualified property under this paragraph, only amounts paid or incurred by the lessor on or after January 1, ~~2005~~ 2007, and prior to the date this section ceases to be operative under paragraph (2) of subdivision (i), shall be taken into account. In the case of any qualified property constructed, reconstructed, or acquired by a lessor pursuant to a binding contract in existence on or prior to January 1, ~~2005~~ 2007, the allocation rule specified in subparagraph (A) of paragraph (1) of subdivision (b) shall apply in determining the original cost to the lessor of qualified property.

(D) Notwithstanding subparagraph (A), in the case of any leasing transaction for which the lessee is allowed the credit under this section and thereafter the lessee (or any party related to the lessee within the meaning of Section 267 or 318 of the Internal Revenue Code) acquires the qualified property from the lessor (or any successor lessor) within one year from the date the qualified property is first used by the lessee under the terms of the lease, the lessee's (or related party's) acquisition of the qualified property from the lessor (or successor lessor) shall be treated as a disposition by the lessee of the qualified property that was subject to the lease under subdivision (g).

(4) For purposes of determining the qualified cost paid or incurred by a lessee in any leasing transaction that is treated as a

1 sale under Part 1 (commencing with Section 6001), the following
2 rules shall apply:

3 (A) Subparagraph (A) of paragraph (1) of subdivision (b) shall
4 be applied by substituting the term “purchase” for the term
5 “construction, reconstruction, or acquisition.”

6 (B) Subparagraph (C) of paragraph (1) of subdivision (b) shall
7 apply.

8 (C) The requirement of subparagraph (B) of paragraph (1) of
9 subdivision (b) shall be treated as satisfied at the time that either
10 the lessor or the qualified taxpayer pays sales or use tax under Part
11 1 (commencing with Section 6001).

12 (5) (A) In the case of any leasing transaction described in
13 paragraph (3), the lessor shall provide a statement to the lessee
14 specifying the amount of the lessor’s original cost of the qualified
15 property and the amount of that cost upon which a sales or use tax
16 was paid within 45 days after the close of the lessee’s taxable year
17 in which the credit is allowable to the lessee under this section.

18 (B) The statement required under subparagraph (A) shall be
19 made available to the Franchise Tax Board upon request.

20 (g) No credit shall be allowed if the qualified property is
21 removed from the state, is disposed of to an unrelated party, or is
22 used for any purpose not qualifying for the credit provided in this
23 section in the same taxable year in which the qualified property is
24 first placed in service in this state. If any qualified property for
25 which a credit is allowed pursuant to this section is thereafter
26 removed from this state, disposed of to an unrelated party, or used
27 for any purpose not qualifying for the credit provided in this
28 section within one year from the date the qualified property is first
29 placed in service in this state, the amount of the credit allowed by
30 this section for that qualified property shall be recaptured by
31 adding that credit amount to the net tax of the qualified taxpayer
32 for the taxable year in which the qualified property is disposed of,
33 removed, or put to an ineligible use.

34 (h) In the case where the credit allowed by this section exceeds
35 the “tax,” the excess may be carried over to reduce the “tax” in
36 the following year, and succeeding years as follows:

37 (1) Except as provided in paragraph (2), for the seven
38 succeeding years if necessary, until the credit is exhausted.

39 (2) In the case of a small business, for the nine succeeding
40 years, if necessary, until the credit is exhausted.

(i) The credit under this section shall be known as the “Career Technical Education Campaign” credit or as the “CTEC” credit.

(j) This section shall become operative on January 1, 2005 2007, and remain in effect only until January 1, 2012 2014, and as of that date is repealed.

~~SEC. 9.— There is hereby appropriated from the General Fund for expenditure in the 2003-04 fiscal year the sum of _____ dollars (\$_____) for allocation to the Franchise Tax Board for its cost to administer this act.~~

~~SEC. 10.—~~

SEC. 6. The Regents of the University of California, in consultation with the State Department of Education and the Franchise Tax Board, and any other organization the university deems appropriate, is requested to conduct an evaluation of the educational and economic effectiveness of the Career Technical Education Campaign credit. It is the desire of the Legislature that the study utilize data from the first four years of the credit’s existence and that the evaluation be provided by December 1, 2012, to the Governor, the Superintendent of Public Instruction, the Franchise Tax Board, the Senate Committee on Revenue and Taxation, the Assembly Committee on Revenue and Taxation, the Senate Committee on Education, and the Assembly Committee on Education.

SEC. 7. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.

CORRECTIONS

Digest — Page 2.